## China's Compliance with WTO Systemic Obligations

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## Institution-related Impediments to Effective Implementation of GATT Article X

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# China's Compliance with WTO Systemic Obligations

## Institution-related Impediments to Effective Implementation of GATT Article X

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# LIST OF ABBREVIATIONS

| | |
|---|---|
| AB | Appellate Body |
| Accession Protocol | Protocol on the Accession of People's Republic of China |
| AIC | Administration of Industry and Commerce |
| ALL | Administrative Litigation Law of China |
| APA | United States Administrative Procedure Act |
| AQSIQ | General Administration of Quality Supervision, Inspection and Quarantine |
| ARO | Agreement on Rules of Origin |
| CCP | Chinese Communist Party |
| COOL | United States—Certain Country of Origin Labelling Requirements |
| Custom Valuation Agreement | Agreement on Implementation of Article VII |
| DSB | Dispute Settlement Body |
| EU | European Union |
| FDA | Food and Drug Administration |
| GAPP | General Administration of Press and Publications |
| GATS | General Agreement on Trade in Services |
| GATT | General Agreement on Tariffs and Trade |
| IP | Intellectual Property |
| IPB | Intellectual Property Bureau |
| IPR | Intellectual Property Rights |
| ITO | International Trade Organization |
| MOA | Ministry of Agriculture |
| MOC | Ministry of Culture |
| MOH | Ministry of Health |
| NAPWC | Office of National Anti-Pornography and Anti-Piracy Working Committee |
| NCA | National Copyright Administration |
| NPC | National People's Congress |

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|---|---|
| PHB | Public Health Bureau |
| PPB | Press and Publication Bureau |
| PPC | Provincial People's Congress |
| PSB | People's Security Bureau |
| QTSB | Quality and Technical Supervision Bureau |
| SAIC State | Administration of Industry and Commerce |
| SARFT | State Administration of Radio, Film and Television |
| SCNPC | Standing Committee of National People's Congress |
| SFDA | State Food and Drug Administration |
| SIPO | State Intellectual Property Office |
| SPS Agreement | Agreement on Sanitary and Phytosanitary Measures |
| STMA | State Tobacco Monopoly Administration |
| TBT Agreement | Agreement on Technical Barriers to Trade |
| TMA | Tobacco Monopoly Administration |
| TRIPS | Agreement on Trade Related Aspects of Intellectual Property Rights |
| TPRM | Trade Policy Review Mechanism |
| TRM | Transitional Review Mechanism for China |
| US | United States |
| WIPO | World Intellectual Property Organization |
| WTO | World Trade Organization |

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# Chapter 1

## Introduction

China's accession to the World Trade Organization (WTO) in 2001 was widely considered a landmark event for the world trading system as WTO membership marks a milestone in China's integration into the international trade order. There is a perception, shared by virtually all knowledgeable observers, that the WTO cannot be truly effective without embracing China as a member, given that the country brings with it the largest population in the world, and has the potential to become the world's largest economy.[1] In the meantime, incorporating such a member, considering its non-market economy and non-rule-of-law legal system, presents a major challenge to the integrity and effectiveness of the rule-oriented system as a whole.

Traditionally, the world trading system was concerned solely with market access relating to border barriers and with economic protectionism involving domestic regulations. Domestic measures restricting trade were permitted so long as they were not discriminatory against imported products or otherwise taken for protectionist purposes. With the establishment of the WTO, which replaced the General Agreement on Tariffs and Trade (GATT) in 1995, the system has expanded to cover many areas that were traditionally under the domestic regulatory domain, such as intellectual property rights, health and safety standards, investment policies and domestic subsidies.[2] The expansion in the case of intellectual property has been dramatic since the agreement covers not only standards for domestic laws, but also detailed provisions for procedures to enforce individual property rights. The WTO rules thus involve commitments for many member countries to what is in effect systemic redesign.[3] New rules also empower the WTO judiciary to engage in a more intrusive review of domestic regulations and national measures considered inconsistent with international standards, regardless of whether they are protectionist in design.[4] The WTO jurisdiction has also been expanded through its accession regime. Countries applying to join the system have been required to take on additional ('WTO-plus') obligations with respect to their

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1 See John H. Jackson, 'The Impact of China's Accession on the WTO', in Deborah Z. Cass, Brett G. Williams and George Barker (ed.), *China and the World Trading System – Entering the New Millennium*, Cambridge University Press 2003, p. 24. On the conclusion of negotiations on China's membership in September 2001, Mike Moore, then Director-General of the WTO, said that 'with China's membership, the WTO will take a major step towards becoming a truly world organization. The near-universal acceptance of its rule-based system will serve a pivotal role in underpinning global economic cooperation.' See also Qinjiang Kong, 'China's WTO Accession: Commitments and Implications', 13 (4) Journal of International Economic Law, 2000; Karen Halverson Cross, 'China's WTO Accession: Economic, Legal and Political Implications', 27 Boston Journal of International and Comparative Law Review, p. 319, 2004.

2 Julia Ya Qin, 'Pushing the Limits of Global Governance: Trading Rights, Censorship and WTO Jurisprudence –A Commentary on the China-Publications Case', *Chinese Journal of International Law*, 2011, pp. 271-322.

3 See Sylvia Ostry, 'WTO Membership for China: to be or not to be – is that the answer?', in Deborah Z. Cass, Brett G. Williams and George Barker (eds.), *China and the World Trading System – Entering the New Millennium*, Cambridge University Press 2003, p. 32.

4 Julia Ya Qin, 'Pushing the Limits of Global Governance', 2011, pp. 271-322.

domestic policies and regulatory systems.[5] This is the context in which China's bid to join the WTO took place. The expansion of the WTO jurisdiction to include both substantive and procedural legal issues made the accession negotiations much more difficult. The accession process presented a complex array of issues associated with China's full integration into the world trading system, especially its compliance capacity, which required a unique response in its accession agreements. During the arduous 15-year negotiation saga, an area that aroused widespread concern among China's trading partners was China's political and legal system, which had significant problems of transparency, due process, authority of law, court independence and capacity and so on.[6] The question of how to establish a rule of law in a country known for a low level of political status and authority for formal legal institutions, and low capacity of courts to handle cases independently and enforce rulings effectively was considered one of main challenges facing China's accession.[7] As these internal conditions might impede China's capacity to ensure meaningful compliance with WTO free trade principles and rules, the country's key WTO trading partners, including the United States (US) and the European Union (EU), insisted on China making fundamental changes to its trade regime and economic governance structure before becoming a member.[8] In the accession agreements, therefore, China undertook extensive and far-reaching WTO-plus obligations in respect of the rule of law and due process requirements, in addition to giving commitments on market access.[9] WTO membership requires China not only to be formally bound by the WTO rules, but also to make conditions in China conducive to these rules' implementation.[10]

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5 WTO-plus obligations refer to provisions in protocols of accession of new members that mandate more stringent requirements than those imposed on other WTO members. The scope and types of WTO-plus obligations vary from country to country. China, among other countries, has committed to include the most extensive and far-reaching WTO-plus obligations in its accession agreements. For a summary of the special commitments of acceding members, see WTO secretariat, Technical Note on the Accession Process, WT/ACC/10/Rev.4/Add.1, 25 May 2010. See also Julia Ya Qin, 'Pushing the Limits of Global Governance', 2011, pp. 271-322; Steve Charnovitz, Mapping the Law of WTO Accession, in Merit E. Janow, Victoria Donaldson and Alan Yanovich (eds.), *The WTO: Governance, Dispute Settlement and Developing Countries*, Juris Publishing, 2008.

6 See, for instance, Yang Guohua and Cheng Jin, 'The Process of China's Accession to the WTO', *Journal of International Economic Law*, 2001, pp. 297-328; Henry Gao, 'China's Participation in the WTO: A Lawyer's Perspective', *11 Singapore Year Book of International Law*, 2007, pp. 1-7; Raj Bhala, 'Enter the Dragon: An Essay on China's WTO Accession Saga', 15 *American University International Law Review*, 2000; Pitman B. Potter, *The Chinese Legal System: Globalization and Local Legal Culture*, Routledge, London, 2001.

7 Sarah Biddulph, 'China's Accession to the WTO – Legal System Transparency and Administrative Reform', in Sylvia Ostry, Alan S. Alexandroff and Rafael Gomez, *China and the Long March to Global Trade: The Accession of China to the World Trade Organization*, 2002, pp. 154-159.

8 Sarah Biddulph, 2002, pp. 154-159.

9 For the detailed discussions of China's WTO-plus Obligations, see Julia Ya Qin, 'WTO-Plus Obligations and Their Implications for the WTO Legal System – An Appraisal of the China Accession Protocol', 37 *Journal of World Trade*, 2003.

10 Xiaohui Wu, 'No Longer Outside, Not Yet Equal: Rethinking China's Membership in the World Trade Organization', *Chinese Journal of International Law*, 2011, pp. 227-270.

## 1.1 COMPLIANCE AND DOMESTIC INSTITUTIONS

The WTO places significant emphasis on domestic conditions for compliance since they are pivotal for the effectiveness of WTO rules at a national level. The compliance theory of international law provides a useful framework for understanding the significance of domestic institutions in compliance. The theory discerns compliance from implementation.[11] According to Oran Young, 'compliance can be said to occur when the actual behavior of a given subject conforms to prescribed behavior, and non-compliance or violation occurs when actual behavior departs significantly from prescribed behavior'.[12] This definition explains that compliance behavior and treaty implementation are two important but different steps for the effectiveness of international agreements.[13] Implementation refers to measures that states take to make international agreements effective in their domestic law.[14] Many international agreements (including the WTO agreements) require national legislation or regulations to become effective at a domestic level.[15] Thus, implementation refers to formal legislation and regulations that countries adopt in order to incorporate treaty obligations.[16]

Compliance goes beyond implementation by requiring *de facto* adherence to the provisions of the international agreement and to the domestic measures implementing these provisions.[17] Compliance is not necessarily achieved even if laws and regulations are *de jure*

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11 Oran Young, *Compliance and Public Authority*, Baltimore: Johns Hopkins Uni. Press, 1979; Beth A. Simmons, 'Compliance with International Agreements', *Annual Review of Political Science* 1998, p. 77.

12 Oran Young, *Compliance and Public Authority*,1979, p. 172.

13 Harold K. Jacobson and Edith Brown Weiss, 'Strengthening Compliance with International Environmental Accords: Preliminary Observations from a Collaborative Project', in Charlotte Ku & Paul F. Diehl (eds.), *International Law: Classic and Contemporary Readings,* Lynne Rienner Publishers, 1998, p. 80.

14 Harold K. Jacobson and Edith Brown Weiss,1998, p. 183.

15 Harold K. Jacobson and Edith Brown Weiss,1998. It should be noted that how an international agreement takes effect within the legal order of a state will depend primarily on a rule of domestic law. The implementation of international law in national courts is often explained from a theoretical perspective in terms of doctrines of incorporation and transformation. Under the doctrine of incorporation, a rule of international law becomes part of national law without the need for express adoption by national courts or legislature. A particular problem may arise with regard to treaties containing non-self-executing provisions; that is, provisions that cannot be directly applied within the national legal system because their implementation requires them to be supplemented by additional national legislation. Whenever treaties contain such provisions, even in those national legal systems where the mere publication of international treaties is sufficient for them to produce effects domestically, implementing legislation first has to be passed. See Antonio Cassese, *International Law*, Oxford University Press, 2nd ed. 2005, pp. 221 & 227. Under the doctrine of transformation, a rule of international law does not become part of national law until it has been transformed into national by state legislation. In practice, a state may adopt a variety of approaches that do not fit neatly into these two categories for applying rules of international law within its legal system. The interaction between international law and national law may be rather more complex than the solutions offered by the two major theories of incorporation and transformation.

16 Harold K. Jacobson and Edith Brown Weiss,1998, p. 180.

17 Harold K. Jacobson and Edith Brown Weiss,1998, p. 183.

adopted. The adoption of domestic laws and regulations are designed to facilitate, but do not in themselves constitute compliance with international agreements. [18] Compliance can thus be defined to include determining both whether a country adheres to the provisions of an international agreement and whether it adheres to the domestic steps that it has taken to implement the agreement. In other words, compliance requires the country to enforce domestic legislation or regulations that have been instituted as part of its implementation efforts in order to make treaty obligations effective at a domestic level.[19] Weak legislation can produce weak compliance, but strong legislation that is unenforced can also have the same effect.[20] It is not sufficient simply to consult domestic legislation to determine whether countries are complying.[21] Compared to implementation, the issue of compliance with international law poses more challenges to the effectiveness of domestic institutions as a whole.

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18 Beth A. Simmons,1998, p. 77.

19 It should be noted that compliance is related to, but not identical to effectiveness of international agreements. Effectiveness requires achievement of the stated objectives of a treaty and addressing the problems that led to the treaty. Countries may be in compliance with a treaty, but the treaty may nevertheless be ineffective in attaining its objectives. A poorly designed treaty could achieve high levels of compliance without having much impact on the problem of concern. While compliance may be necessary for effectiveness, there is no reason to consider it sufficient. Beth A. Simmons,1998, p. 78; Harold K. Jacobson and Edith Brown Weiss,1998, p. 184.

20 Harold K. Jacobson and Edith Brown Weiss,1998, p. 183.

21 Harold K. Jacobson and Edith Brown Weiss,1998, p. 179.

There are many factors affecting compliance, according to the various approaches adopted in compliance discussions.[22] The functionalist approaches focuses particularly on a range of domestic conditions that can contribute to or detract from compliance.[23] Jacobson and Brown Weiss, as representatives of the functionalist approach,[24] summarize factors affecting compliance with international obligations that they identified through their research of environmental accords and their studies on the impact of domestic conditions in compliance.[25] Although these studies were based on compliance with international environmental accords, the findings may offer valuable insight into compliance with all types

22 According to Beth Simmons's review, there are four perspectives or approaches to discussing the conditions under which states comply with international agreements: realist theory, rational functionalism, domestic regime-based explanations, and normative approaches. From a realist perspective, power, rather than law, has traditionally been the primary determinant of the course of interstate relations, while international law is merely an epiphenomenon of interests or is made effective only through the balance of power. For the most part, realist perspectives focus on the fundamental variables of power and interest, rarely inquiring further into state's compliance with international agreements. Functionalist approaches view international agreements as a way to address a perceived need: international agreements are made because states want to resolve common problems that they find difficult to resolve in any other way. The starting point for functionalist explanations of international agreements and compliance is states' inability to resolve a problem without an international device. In these circumstances, actors may have incentives not only to enter into international agreements, but also to comply with them in order to resolve an intractable domestic problem. In this view, international agreements place a desired constraint on policy where domestic politics alone have proved socially suboptimal. One of the most tangible sources of suboptimal social behavior is domestic administrative or technical incapacities. A host of studies, many relating to compliance with environmental accords, point to the inability (as distinct from the unwillingness) of governments to comply with international obligations. In domestic regime-based formulations, which can also be regarded as democratic legalist, regime type is crucial to understating the role of law in interstate relations. While functionalist literature focuses on the range of domestic conditions that can contribute to or detract from compliance, the democratic legalist approach looks at the distinctive features of democratic regimes that tend to bind them into a 'zone of law' in the way they conduct their foreign relations. The thrust of this approach is that democratic countries are expected to be more willing to use legal institutions to regulate international behavior and settle disputes, and to comply more readily with these agreements once they have been made. Countries with independent judiciaries are more likely to trust and respect international judicial processes than those lacking domestic experience with such institutions. Normative approaches are present to some degree in the observation that democratic norms relating to the rule of law may influence governments' attitudes toward compliance with international law. These approaches focus on the force of ideas, beliefs, and standards of appropriate behavior as major influences on governments' willingness to comply with international agreements. Beth A. Simmons, 1998.

23 Beth A. Simmons,1998, p. 83.

24 Beth A. Simmons,1998, p. 83.

25 Harold K. Jacobson and Edith Brown Weiss,1998; Edith Brown Weiss, 'Strengthening National Compliance with Trade Law: Insights from Environment', in Marco Bronckers and Reinhard Quick (eds.), *New Directions in International Economic Law*, Kluwer Law International, 2000.

of agreements, including trade. Capacity to comply[26] covers many aspects of a country's social, cultural, political and economic environment.[27] Certain questions have been raised: are there, for instance, cultural traditions that influence how a country complies? What difference does it make whether the country has a market economy or a planned economy? What are the effects of the political system? How strong and effective is the bureaucracy, and what difference does it make? What is the nature of the legal system? According to functionalist studies, these domestic conditions, which are institution-related, can affect a country's capacity to comply.

The relationship between institution-related factors and capacity to comply has also been demonstrated in literature discussing the administrative capacity to comply.[28] Administrative capacity includes not only resource-related factors such as knowledge, trained personnel and adequate financial resources,[29] but also institution-related factors such as whether a state has the appropriate domestic regulatory bodies to issue rules and regulations, and to monitor their enforcement.[30] Countries that have stronger administrative capacity can do a better job.[31] Administrative capacity involves the nature of countries' political systems, administrative structures, and regulatory bureaucracies.[32] Administrative structure matters because whereas in some nations, for example, responsibility for implementation rests with central governmental units, in other nations, such as those with a federal government, it is handled by provincial or local governments.[33] In these situations, the provincial or local governments may play a more important role in ensuring compliance.

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26 Domestic intent and capacity are recognized as critical variables in compliance. Edith Brown Weiss, 2000, p. 458. Oran Young also emphasizes that the effectiveness of international institutions depends on the willingness of governments to comply with the relevant rules, as well as on the capacity of governments to implement institutional arrangements within their jurisdictions. Oran Young, 'The Effectiveness of International Institutions: Hard Cases and Critical Variables', in James N. Rosenau and Ernst-Otto Czempiel (eds.), *Governance without Government: Order and Changes in World Politics*, Cambridge University Press, 1992, p. 183.
Beth A. Simmons,1998, p. 83; David Vogel and Timothy Kessler, 'How Compliance Happens and Doesn't Happen Domestically', in Edith Brown Weiss & Harold K. Jacobson (eds.), *Engaging Countries: Strengthening Compliance with International Environmental Accords*, MIT Press, 1998, p. 20.

27 Harold K. Jacobson and Edith Brown Weiss,1998, pp. 185-186.

28 Beth A. Simmons,1998, p. 83; David Vogel and Timothy Kessler,1998, p. 20.

29 Beth A. Simmons,1998, p. 83. The resource constraints can be represented by the lack of financial support, necessary techniques and trained personnel. Most governments face severe resource constraints that limit their ability to apply the provisions of agreements to areas and activities under their jurisdiction. This is obviously true of the governments in developing countries that have to contend with a wide range of pressing problems. Oran Young, 'The Effectiveness of International Institutions',1992, p. 183.

30 David Vogel and Timothy Kessler,1998, p. 20.

31 Harold K. Jacobson and Edith Brown Weiss,1998, p. 200.

32 David Vogel and Timothy Kessler,1998, pp. 20-23.

33 David Vogel and Timothy Kessler,1998, p. 22.

## 1.2 SYSTEMIC OBLIGATIONS IN THE WTO – GATT ARTICLE X

The WTO contains a series of systemic obligations that impose requirements on domestic institutions. The systemic obligations discussed in this study are those that stand in contrast to substantive obligations.[34] Whereas substantive obligations relate to specific acts or conducts and set out the standards of treatment to be accorded by one WTO member to goods, services and intellectual property rights originating in another WTO member,[35] systemic obligations are those that perform a systemic function[36] and exert a systemic impact on domestic institutions. Although the WTO laws do not give rise to general institutional obligations, some institution-related obligations can be found in various specific trade agreements.

The highest concentration of systemic obligations can be found in Article X of the GATT. This includes obligations to administer national laws in a uniform and impartial manner,[37] to ensure transparency in respect of national laws through their publication and notification to the WTO,[38] and to make specified procedures and remedies for administrative actions (for example, procedures for judicial review of administrative acts) available under national laws.[39] Similar obligations can be found in various WTO agreements.[40] For example, the commitment on uniform administration of national laws provided in GATT Article X:3(a) requires that 'Each Member shall administer in a uniform, impartial and reasonable manner all its laws, regulations, decisions and rulings of the kind described in paragraph 1 of this

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34 Bhuiyan characterizes WTO obligations into systemic obligations and substantive obligations. Sharif Bhuiyan, *National Law in WTO Law – Effectiveness and Good Governance in the World Trading System*, Cambridge University Press, 2007, p. 43. It should be noted that systemic obligations are also characterized as rule-of-law obligations. By incorporating many rule-of-law concepts, such as transparency, uniform and objective administration of laws, effective enforcement and judicial review, these obligations, have been described as rule-of-law obligations. See, for instance, Warren Maruyama, 'The WTO: Domestic Regulation and the Challenge of Shaping Trade', *International Lawyer*, vol. 37, issue 3, 2003, p. 681; Leila Choukroune, 'China-WTO, Rule of Law Through the Opening to International Trade?', *International Business Law Journal*, No. 6, 2002; Paolo D. Farab, 'Five Years of China's WTO Membership – EU and US Perspective on China's Compliance with Transparency Commitments and the Transitional Review Mechanism', *Legal Issues of Economic Integration*, 33(3), 2006, p. 265.

35 Sharif Bhuiyan, 2007, p. 43.

36 Sharif Bhuiyan, 2007, p. 43.

37 Article X: 3(a) of General Agreement of Trade in Goods (GATT). This obligation is emphasized in the Protocol on the Accession of People's Republic of China (Accession Protocol) as 'uniform implementation of trade policies and laws'.

38 Article X: 1 of the GATT.

39 Article X: 3(b) of the GATT, Article VI: 2(a) of the General Agreement on Trade in Services (GATS), and Article 41 (4) of the Agreement on Trade-related aspects of Intellectual Property Rights. A detailed discussion of these systemic obligations is provided in Chapters III, IV and V.

40 Sharif Bhuiyan, 2007, p. 75.

Article'.[41] This requirement can also be found in the Agreement on Rules of Origin (ARO),[42] the Agreement on Import Licensing Procedures (Licensing Agreement)[43] and the General Agreement on Trade in Services (GATS).[44] Although these provisions variously require 'uniform', 'impartial', 'reasonable', 'consistent', 'neutral', 'objective', 'fair', and 'equitable' administration of national laws, the differences are not of much significance according to the interpretation of the Appellate Body.[45]

It is interesting to note that although Article X has now been recognized as an important due process provision for the compliance of the WTO rules, the inclusion of this Article when GATT was established in 1947 seemed more of a coincidence than an intended arrangement and occurred without the full recognition of the importance of domestic institutions in the trading system that Article X currently demonstrates. The idea of procedural requirements as a norm for the trading system was based on US administrative law.[46] Article 15 of the September 1946 State Department document 'Suggested Charter for an International Trade Organization of the United Nations' was entitled 'Publication and Administration of Trade Regulations – Advance Notice of Restrictive Regulations'.[47] This Article was ultimately incorporated into the Havana Charter for the International Trade Organization as Article 38 and also as Article X of the GATT, which survived the demise of the International Trade Organization.[48] The language of Article X does not vary significantly from the original State Department document drafted by the US in 1946.[49] Although most of the other Articles in the original US proposals for international trade regulation involved considerable haggling and compromise, the inclusion of Article X appears to have been non-controversial.[50] There were two possible reasons for this. Firstly, the delegations at Havana saw Article X as not

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41 Article X: 1 of the GATT describes the laws and regulations as 'laws, regulations, judicial decisions and administrative rulings of general applications, made effective by any contracting party, pertaining to the classification or the calculation of products for customs purposes, or to rates of duty, taxes or other charges, or the requirements, restrictions or prohibitions on imports or exports or on the transfer of payments therefore, or affecting their sale, distribution, transportation, insurance, warehousing inspection, exhibition, processing, mixing or other use.'

42 Article 3(d) of the ARO provides that Members shall ensure that the rules of origin are administered in a consistent, uniform, impartial and reasonable manner.

43 Article 1.3 of the Licensing Agreement provides that the rules of import licensing procedures shall be neutral in application and administered in a fair and equitable manner.

44 Article VI: 1 of the GATS provides that Members shall ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner.

45 Sharif Bhuiyan, 2007, pp. 75-76.

46 Sylvia Ostry, 'China and the WTO: Transparency Issue', 3 *UCL*A *Journal of International Law and Foreign Affairs,* 1, 1998.

47 U.S. Dept. of State, Suggested Charter for an International Trade Organization of the United Nations (1946). Sylvia Ostry, 'China and the WTO: Transparency Issue',1998.

48 U.S. Dept. of State, Havana Charter for an International Trade Organization (1948), Pub. No. 3206.

49 Sylvia Ostry, 'China and the WTO: Transparency Issue',1998.

50 Sylvia Ostry, 'China and the WTO: Transparency Issue',1998.

imposing any obligations on them that they did not already comply with.[51] Secondly, Article X was deemed by the drafters of the new system to be, in some sense, insignificant because the main focus of trade policy at the time was on seeking to reduce the border barriers erected during the 1930s.[52] Trade regulation was limited to border measures, which had little to do with characteristics of domestic institutions. Border barriers such as tariffs and quotas, for instance, are for the most part relatively transparent. Since the Tokyo Round, however, the focus of the trading system has shifted away from reducing border barriers and towards regulating domestic policy. Since the expansion of the mandates of the trading system, barriers to trade have no longer been controlled by borders, but instead involve domestic regulatory regimes and institutional infrastructure, as seen in respect of market access in the areas of services, intellectual property, and investment. As a result, the systemic obligations represented by Article X GATT have gained in importance in the world trading system.

Systemic obligations act as a *sine qua non* of the effectiveness of WTO substantive obligations. It appears from the nature of these obligations that they relate to the implementation of substantive obligations.[53] They provide guarantees of non-discrimination, substantive equality, proportionality, and judicial protection of treaty obligations at a national level.[54] Although these obligations were established on a case-by-case basis, rather than in any systemic or organized fashion,[55] they indeed provide useful bases for fairness and procedural due process[56] that are indispensable for effective implementation of all the other WTO obligations at national levels. They require a member to establish an equitable and effective domestic environment within which the substantive obligations can be implemented. Furthermore, they are key elements in enhancing the predictability of a trading system from the perspective of protecting individual traders. Foreign trading partners seek certain assurances when operating in foreign countries, including respect for the rule of law.[57] Without stable and predictable conditions, it is more difficult for foreign companies to operate successfully in such countries.[58]

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51 The Canadian delegation noted, for example, that Article 38 of the Havana Charter for the ITO, which later became GATT Article X, had not been altered and nor were any interpretive notes required. It further noted that 'This Article imposes no obligations upon Canada not already complied with, and the general benefit to international trade needs no elaboration.' Canadian Legation, Report of the Canadian Delegation to the United Nations Conference on Trade and Employment at Havana, 32, 13 July 1948; Sylvia Ostry, 'China and the WTO: Transparency Issue', 1998.

52 Sylvia Ostry, 'China and the WTO: Transparency Issue', 1998.

53 Richard Frimpong Oppong, 'Book Review on National Law in WTO Law-Effectiveness and Good Governance in the World Trading System', *Journal of International Economic Law*, 11(2), 2008, p. 502.

54 Richard Frimpong Oppong, 2008, p. 502.

55 Warren Maruyama, 2003, p. 685.

56 Warren Maruyama, 2003, p. 685.

57 Warren Maruyama, 2003, p. 677.

58 Warren Maruyama, 2003, p. 677.

## 1.3 DOMESTIC INSTITUTIONS: OBSTACLES REMAINING 10 YEARS AFTER CHINA'S ACCESSION

The first decade of China's membership of the WTO progressed smoothly. China made substantial progress in modifying its legal system in order to comply with its WTO commitments, which require a comprehensive overhaul of relevant laws, regulations and procedures. The WTO dispute settlement system has not been overwhelmed by cases claiming non-compliance by China, thus assuaging concerns at the time of China's entry that it would cause a huge volume of litigation – 'case flood'[59] – that could even threaten the efficacy of the WTO dispute settlement mechanism. The caseload attributable to China in recent years should be seen as commensurate to its size.[60]

Although China has undergone dramatic changes to implement its WTO commitments, the overall picture is complex. Debates continue as to whether China has adequately complied with both the letter and spirit of its obligations under the WTO agreements. The problematic enforcement of intellectual property protection, which has been a constant source of complaints, is most symbolic in demonstrating the gap between the law on paper and the law in practice in China. The reports of the WTO trade policy review on China's compliance also show many disputed issues to be closely related to domestic institution-related conditions, such as transparency and the role of government in economic activities.[61]

In March 2011, China failed to comply, for the first time, with the adverse WTO ruling in *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications*

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59 John H. Jackson, 2003, p. 27.

60 As at October 2011, there were a total of 23 cases in which China was the respondent. By comparison, the EU had 70 cases, the US 113 cases, and Japan 15 cases as the respondent. http://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm

61 WTO, Trade Policy Review Body, 'Trade Policy Review on People's Republic of China, Minutes of Meeting', WT/TPR/M/161, 6 June 2006; WTO, Trade Policy Review Body, 'Trade Policy Review on People's Republic of China, Report by Secretariat', WT/TPR/S/161, 28 February 2006. See also 'China's Implementation of its World Trade Organization Commitments', Written Testimony by US-China Business Council, submitted in response of the office of the US Trade Representatives' request for comment and notice of public hearing concerning China's compliance with WTO commitments, Federal Register, Pages 42886-42887, 28 July 2006.

*and Audiovisual Entertainment Products* (*China-Publications*) before the deadline.[62] To comply with the WTO ruling the Chinese government would have had to embark on serious systemic reforms in its existing censorship of the cultural industry, under which only selected state-owned entities are authorized to import cultural and information products, and the government is able to keep its censorship process non-transparent and with the maximum level of flexibility and efficacy desired. The WTO rulings did not question the necessity of the existence of censorship on cultural products. Rather, they questioned the necessity of restricting trading rights to selected state-owned entities in performance of the censorship function. Thus, China was required to grant the right of importing cultural products to all enterprises and individuals in China, including those who may also have the ability to conduct censorship/content review, but who will have a less restrictive effect on trade. Although some restrictions on trading rights have since been removed from the relevant legal provisions (such as the formal requirement for state ownership of importers), this will not result in foreign investors automatically being granted the right to import cultural products. The government has retained full discretion in approving importers, and the actual criteria for approval remain unclear.

While the WTO rulings do not require a change in China's political or legal institutions, they do require a change in the way these institutions operate. As required in the WTO rulings in the *China-Publications* case, fair administration of trading rights necessitates substantial reform in China's domestic regulatory and political regime. This once again demonstrates that the effectiveness of substantive WTO trading rules is heavily reliant on domestic institution-related factors. However, China's failure to comply with the far-reaching WTO rulings recalls the questions that was raised at the time of China's entry: 'Has China, in the protocol process, been pushed too far – too far for its own good, given the adjustment that it is facing, and too far for the West's own good in developing a more constructive relationship with China?'[63] Would the trend of expanding the WTO's jurisdiction help the multilateral trading system to achieve ultimate effectiveness? Would mandating a ruling calling for changes of an institutional nature in the domestic system of a sovereign nation push the limit of WTO governance too far, and would its authority and legitimacy eventually be undermined if such a ruling were not complied with?

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62 Prior to this case, China had a perfect record of complying with adverse WTO decisions. In the first two cases in which its measures were found to be WTO-inconsistent, China fully implemented DSB rulings. See Appellate Body Report, China – Measures Affecting Imports of Automobile Part, WT/DS339, 340,342/AB/R, adopted on 12 January 2009; Panel Report, China – Measures Affecting the Protection and Enforcement of Intellectual Property Rights, WT/DS362/R, adopted on 20 March 2009. China was given 14 months, or until 19 March 2011, to comply with the WTO rulings in the China-Publications case. By April 2011, China had issued and proposed several amendments to its regulations concerning the right to import cultural products. These amendments, however, have all fallen short of meeting the WTO requirements. For details, see Julia Ya Qin, 'Pushing the Limits of Global Governance', pp. 271-322, 2011.

63 John H. Jackson, 2003, p. 30.

Moreover, in the early stage of WTO dispute settlement, the Dispute Settlement Body (DSB) was reluctant to issue rulings on GATT Article X due to its intrusive and far-reaching requirements, and complaints under GATT Article X were regarded only as add-on or subsidiary complaints attached to complaints on more substantive obligations. However, the relative prominence of GATT Article X in recent trade disputes shows that the DSB has now opted to build more solid jurisprudence on this Article. The Panel's ruling in the recent case of *United States – Certain Country of Origin Labelling Requirements(COOL)*, which confirms a violation of Article X:3(a), demonstrates a tendency for Article X obligations to be more strictly applied. While this can be viewed as a good sign for the development of WTO as a rule-oriented body and for the development of DSB jurisprudence, it may not be a good sign if we take China's compliance capacity into consideration. How likely is China to comply with DSB rulings? Is it still a good sign for the development of the WTO if China fails to comply? In the *China-Publications* case China notified the WTO of its difficulty in complying with the DSB ruling by stating that, 'China hoped that relevant WTO Members could understand the *difficult and complicated situation* China is facing during the process of implementation considering the dispute is embodied with more complexity and sensitivity than other disputes'.[64] Without an in-depth understanding of the *difficult and complicated situation* of China, it is impossible to make a sound judgment of the broad questions raised above.

## 1.4 MAIN RESEARCH QUESTIONS AND METHOD

It is in the above context that this study attempts to probe into legal difficulties existing in China's domestic institutions with regard to its WTO compliance. Examining compliance with the systemic obligations in GATT Article X provides an ideal setting for this research because the difficulties in complying with the obligations that impose immediate requirements on domestic institutions are representational of overall institutional obstacles to China's WTO compliance. Thus, the main research question in this thesis is the institution-related legal difficulties in China's compliance with GATT Article X; in other words, with the requirement of transparency, uniform administration of application of laws, and judicial review.

Through an in-depth examination of the difficulties China faces in adapting to those intrusive requirements, this study provides a specific example of the extent of the challenges the WTO faces in seeking to incorporate a member such as China, and contributes to answering the broad questions raised above, which are important for the development of the WTO. It should be noted that this study is not seeking to answer whether China actually complies with the systemic obligations. Instead, it seeks to find out why this compliance is difficult by focusing on the broader significance of obstacles to it, in so far as they illustrate the institutional nature of China's integration into the world trading system. Thus, this study analyzes, one by one, how institution-related difficulties are impeding China's compliance

64 WT/DS363/17/Add.2, 15 March 2011.

with three systemic obligations provided for in Article X GATT. The problematic enforcement of intellectual property rights (IPR) is also discussed as a case study demonstrating all the various difficulties.

Although there has been extensive discussion of China's implementation of its WTO commitments,[65] most existing literature deals with only one or a few specific WTO agreements or commitments, such as investment, agriculture or banking.[66] There is a relative dearth of comprehensive and in-depth studies on internal barriers affecting compliance with systemic WTO obligations. While implementation in each different trade area may give rise to its own particular set of problems, there are some general systemic obstacles that cut across various areas, albeit with varying degrees of relevance and importance in the different areas. From a practical perspective, this study will help China's trading partners to gain a sounder understanding of the political and institutional barriers jeopardizing the country's compliance with its WTO commitments and thereby create more reasonable expectations of negotiations or dispute settlements involving China.

This study is mainly based on literature research. The primary sources used include firstly WTO law, rulings and reports, as well as Chinese laws, regulations, rules, and China's accession commitments; secondly, Chinese national, provincial and county-level statistical yearbooks; thirdly, governmental investigation reports and testimony, mainly from China and the US; fourthly, newspaper reports published in Chinese. It should be noted that the paucity of published primary sources is a common obstacle in English-language research on Chinese law. Precise and reliable information on China is hard to find. This problem has forced researchers to look for other sources of information. In the early days,

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65 See, for example, Sylvia Ostry, Alan S. Alexandroff and Rafael Gomez, *China and the Long March to Global Trade: the Accession of China to the World Trade Organization*, London: Routledge, 2002; Deborah Z. Cass, Brett Gerard Williams, George Robert Barker, *China and the World Trading System: Entering the New Millennium*, Cambridge UK, New York: Cambridge University Press, 2003; Qingjiang Kong, 'Enforcement of WTO Agreements in China', *Journal of World Trade*, vol. 35, issue 6 (2001); Paul Tiers, 'Challenge of WTO Implementation: Lessons from China's Deep Integration into International Trade Regime', *Journal of Contemporary China*, vol. 11, issue 32, 2002; Penelope B. Prime, 'China's WTO Compliance: Commitments and Progress in Initial Stage', in Hung-Gay Fung, Changhong Pei, Kevin H. Zhang (eds.), *China and the Challenge of Economic Globalization: the Impact of the WTO Membership*, Armonk, NY: Sharpe, 2006; Yu Min-you, 'China's Compliance with WTO Commitments: A Compliance Theory Analysis', in Chen Huiping and Eric E. Bergsten (eds.), *International Economic Law and China in its Economic Transition*, Buffalo, NY: Hein, 2007; Henry Gao and Donald Lewis, *China's Participation in the WTO*, London: Cameron May, 2005.

66 See, for example, Wei Wang, 'Implementation of China's WTO Commitments: the Compliance Issue in Banking', in James R. Bath (ed.), *Financial Restructuring and Reform in Post-WTO China*, Alphen aan den Rijn: Kluwer Law International, 2007; Frederick W. Crook, 'The WTO's Impact on China's Agricultural Sector', *China Business Review*, vol. 29, issue 2, 2002; K.X. Li, Kevin Culinane and Cheng Jin, 'The Application of WTO Rules in China and the Implications for Foreign Direct Investment', *Journal of World Investment*, vol. 4, issue 2, 2003, pp. 343-361; Qin Julia Ya and Huang Dongli, 'Trade, Investment and Beyond: the Impact of WTO Accession on China's Legal System', in Donald C. Clarke (ed.), *China's Legal System: New Developments, New Challenges*, Stanford, CA: Stanford University Press, 2008, pp. 166-190.

some researchers, who had contacts with employees or former employees of Chinese governmental bodies, based their research mainly on interviews in order to obtain access to internal documents. However, the most frequently used sources remain books and periodicals in English and Chinese. The main flaw in using secondary sources in Chinese is that although a lot of statistics and cases are referred to, the origins of these data are either from another secondary source or unknown. In one of the most comprehensive studies on the Chinese legal system, Professor Donald C. Clarke of the University of Washington Law School conceded that the various statistics contained in his study might not be accurate or fully reliable.[67] Despite the shortcomings in the Chinese sources, it is still possible to construct a range of possible findings using available resources and statistics. In many cases, this information indicates the existence or severity of the problem in China, even though we do not know how reliable the resources are or have the sources to verify them. This study, therefore, uses many secondary sources, while also referring to primary sources wherever possible.

This thesis consists of five chapters, the first of which is the introduction. Chapter two examines China's compliance with the first systemic obligation – the transparency requirement with respect to the publication of national laws and administrative regulations. It demonstrates the importance of transparency as a systemic obligation in ensuring the implementation of substantive obligations under the WTO. It also explores China's domestic legislative regime and observes specific difficulties in the administrative and legal institutions that may render Chinese legislation incapable of ensuring transparency.

Chapter three discusses China's compliance with the second systemic obligation – uniform administration of national laws. It analyzes the importance of this obligation in the WTO agreements and explains why this is particularly emphasized in China's accession documents. It discusses the problematic practice of uniform administration of implementation of laws and trade policies in China. It specifically examines the problem of market fragmentation resulting from the lack of a uniform administration, and analyzes how this reversely undermines the effectiveness of core WTO obligations such as national treatment and non-discrimination.

Chapter four examines China's compliance with the third systemic obligation – judicial review, which requires China to provide review procedures and remedies on administrative actions within its domestic judicial system. After reviewing the development and practice of judicial review in China, this chapter firstly discusses how the general structural defects

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67 In, for example, the discussion of execution problem, he stated that 'How bad are things really? It turns out that good statistics are simply not reliable on this matter. An extensive review of the literature failed to turn up a single serious study using well-defined categories.' Donald C. Clarke, 'Power and Politics in the Chinese Court System: The Enforcement of Civil Judgments', *Columbia Journal of Asian Law*, vol. 10, No. 1, 1996, p. 27.

in the Chinese judicial system affect the effectiveness of judicial review in China. It then examines the more specific and technical obstacles to judicial review caused by problems in the judicial review legislation. Lastly it evaluates China's efforts to improve the effectiveness of judicial review, specifically for foreign trade-related matters, and analyzes whether this is a feasible way of making China more compliant with the WTO requirement without major institutional adjustments.

No set of WTO compliance difficulties illustrates the basic dynamics of institutional impediments faced by China better than those in IPR enforcement. After examining China's compliance with three systemic obligations, chapter five therefore discusses the problems of effective enforcement of IPR as a case study to illustrate how the institutional barriers discussed in the previous chapters may undermine the effectiveness of substantive WTO obligations. Although numerous factors have contributed to the failure of IPR protection in China, this chapter discusses the impact of three institution-related factors only: transparency, uniform administration, and judicial review.

# Chapter 2

## Compliance with Transparency Requirements in Legislative Regime

## 2.1 INTRODUCTION

As one of the main pillars of the world trading system, the transparency principle[68] articulated in Article X:1 of the GATT imposes an obligation on WTO members to publish all applicable laws and regulations as follows:

> Laws, regulations, judicial decisions and administrative rulings of general application, made effective by any contracting party, pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges, or to requirements, restrictions or prohibitions on imports or exports or on the transfer of payments therefore, or affecting their sale, distribution, transportation, insurance, warehousing inspection, exhibition, processing, mixing or other use, shall be published promptly in such a manner as to enable governments and traders to become acquainted with them. Agreements affecting international trade policy which are in force between the government or a governmental agency of any contracting party and the government or governmental agency of any other contracting party shall also be published …

Transparency is essential for the trading system in that it is usually cited as the core principle underpinning the rule of law, which is the foundation of the WTO regime. For WTO members, acceptance of obligations to comply with the transparency provisions is necessary to increase competitiveness in the world economy.[69] Transparent laws, administrative decisions, and procedures undoubtedly encourage foreign investment, whereas non-transparent laws and regulations can create barriers to trade, particularly to imports.[70] In practice, traders seeking access to a market must have adequate information on applicable rules so that they can base their decisions on an accurate assessment of the potential costs, risks and market

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68 The principle of transparency is relevant to the WTO system in the context of external, internal, and regulatory transparency. External transparency relates to the ability of civil society to see the work of the WTO, including the WTO procedures and decisions, while internal transparency reflects the equal access of WTO members, particularly smaller and developing countries, to the work of the WTO. Regulatory transparency means transparency in law-making and administration of a WTO member at its domestic level. Robert Wolfe, 'Regulatory Transparency, Developing Countries and the WTO', 2, *World Trade Review* 157, 2003.The discussion of the principle of transparency in this chapter focuses only on regulatory transparency.

69 Ljiljana Biukovic, 'Selective Adaptation of WTO Transparency Norms and Local Practices in China and Japan', *Journal of International Economic Law* 11(4), 2008, pp. 803-825.

70 Ljiljana Biukovic, 2008, pp. 803-825.

opportunities.[71] If they cannot find out such information, trade is less likely to occur.[72] Thus, transparency is fundamentally important to WTO's goal of expanding international trade. Moreover, transparency facilitates rule enforcement by helping members to verify that other members are fulfilling their basic WTO obligations.[73] This reinforces members' confidence in the WTO system and facilitates future negotiations to the extent that members believe that WTO commitments will actually be implemented.[74]

The text of the domestic regulatory transparency requirement provided in Article X:1 GATT appears intrusive as it has the capacity for direct impact on the field of members' administrative law. Acceptance of the rule of transparency requires serious commitments on the part of members and leads to legal reforms involving the adoption of a Western system of law.[75] Concepts underpinning transparency are at the core of liberal democracies and open market economies, but not in traditional Asian countries.[76] In China, the transparency principle has still to take root in its administrative legal regime. For this reason, the WTO-plus transparency obligations – in other words, commitments going beyond the requirements provided for in Article X:1 – have been imposed on China in order to ensure that whenever WTO rules are inadequate, WTO-plus obligations will fill the gap. However, the WTO-plus obligations will not necessarily ensure better compliance with transparency if China already has difficulties in complying with the basic transparency requirement. Although China made some legislative and institutional efforts to enhance transparency after its accession, the lack of transparency in its domestic regulatory regime remains a constant source of complaints. Despite the fact that the 'publication' requirement is explicitly provided for in Chinese law, many legal enactments are not publicly accessible in practice. Requesting China to revise its legislation or publish all laws in one national journal, which is the approach that the trading partners have adopted, seems unlikely to achieve any substantial improvement. Rather than analyzing the specific efforts China has made to enhance transparency, this chapter therefore attempts to explore obstacles to transparency in a broader context, related to the institutional settings, in order to gain some understanding of the substance of the difficulties faced by China. It addresses the institutional obstacles to regulatory transparency from three perspectives:

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71 Vera Nicholas-Gervais et al, 'Background Report on Enhancing Market Openness through Regulatory Reform', in *OECD Reviews of Regulatory Reform: Regulatory Reform in the United States* 230, 1999; Christopher Duncan, 'Out of Conformity, China's Capacity to Implement World Trade Organization Dispute Settlement Body Decisions after Accession', *American University International Law Review*, 2002.

72 William Davey, *Enforcing World Trade Rules: Essays on WTO Dispute Settlement and GATT Obligations*, Cameron May, 2006, p. 301.

73 William Davey, 2006, p. 301.

74 Christopher Duncan, 2002; William Davey, 2006, p. 301.

75 Sylvia Ostry, 'China and the WTO: Transparency Issue',1998.

76 Randall Peerenboom, *China's Long March to Rule of Law*, Cambridge University Press, 2002.

- Non-transparency caused by problems in the Chinese formal legislative system in general;
- Specific difficulties caused by the existence of informal laws that hinder fulfillment of the publication requirement;
- Influence of legal culture.

Part I outlines the transparency requirement in the WTO agreements and the way it is interpreted in the WTO adjudication, while also sketching China's commitments on transparency. Parts II, III and IV discuss the institution-related obstacles to transparency from the above three perspectives.

## 2.2 TRANSPARENCY REQUIREMENT IN THE WTO AGREEMENTS AND CHINA'S COMMITMENTS

Normally described as the sunshine strategy, transparency is employed, to varying degrees[77], as one of three major legal strategies[78] designed to encourage compliance with international agreements in all fields of international law.[79] Generally speaking, there are three reasons for transparency's importance in international law. Firstly, it makes non-compliance more apparent to the public, NGOs and other member countries, as well as making it easier for international and national actors to take action to encourage and enforce accountability and compliance.[80] Secondly, transparency deters non-compliance with a treaty by allowing failure to comply to be associated with public visibility.[81] It can act as a deterrent because behavior deviating from a treaty will be discovered, and 'even when direct retaliation seems unlikely, exposure alone can cause behavior to change'.[82] Lastly, it promotes compliance

77 Harold K. Jacobson & Edith Brown Weiss, 'Accessing the Record and Designing Strategies to Engage Countries', in Edith Brown Weiss & Harold K. Jacobson eds., *Engaging Countries: Strengthening Compliance with International Environment Accords*, MIT Press, 1998, p. 542.

78 The other two are positive incentives (to encourages states to comply with the obligations), such as financial and technical assistance, and coercive measures, such as sanctions, penalties to punish non-compliance. See Harold K. Jacobson & Edith Brown Weiss, 'Accessing the Record and Designing Strategies to Engage Countries', in Edith Brown Weiss & Harold K. Jacobson (eds.), *Engaging Countries: Strengthening Compliance with International Environment Accords*, MIT Press, 1998, p. 542.

79 Edith Brown Weiss, 2000.

80 Harold K. Jacobson & Edith Brown Weiss, 'A Framework for Analysis', in Edith Brown Weiss & Harold K. Jacobson (eds.), *Engaging Countries: Strengthening Compliance with International Environment Accords*, MIT Press, 1998, p. 4. Mark R. Goldschmidt, 'The Role of Transparency and Public Participation in International Environmental Agreements: The North American Agreement on Environmental Cooperation', *Boston College Environmental Affairs Law Review*, vol. 29, 2002.

81 Abram Chayes, 'Managing Compliance: A comparative Perspective', in Edith Brown Weiss & Harold K. Jacobson (eds.), *Engaging Countries: Strengthening Compliance with International Environment Accords*, MIT Press, 1998, p. 44.

82 Abram Chayes,1998, p. 44.

by allowing other parties to observe deviations from prescribed conduct and by requiring those deviations to be accounted for and justified.[83]

## 2.2.1 Transparency Requirement in the WTO Agreements and its Enforcement

### *2.2.1.1 Transparency Requirement and GATT Article X:1*

While transparency can broadly relate to the openness of a government's political system, to the nature of participation in the decision-making process, and to the access to and distribution of information, the domestic regulatory transparency requirement provided for in the WTO agreements limits itself to minimum standards of transparency, primarily by imposing the 'publication' obligation on members. As the most representative transparency provision in the WTO agreements, GATT Article X:1 sets out the general publication requirement, while Article X:2 also states that no measure of general application may be enforced before such measure has been officially published. The idea of transparency as a norm for the trading system is recognized as being based on US administrative law,[84] and the language of Article X was borrowed from the 1946 US Administrative Procedure Act (APA).[85] It was in 1946, while the negotiations for the new trading system were underway, that the US Congress codified views on the law of administrative procedure by passing the APA.[86] Article 15 of the September 1946 State Department document 'Suggested Charter for an International Trade Organization of the United Nations' was entitled 'Publication and Administration of Trade Regulations – Advance Notice of Restrictive Regulations'.[87] This Article was ultimately incorporated into the Havana Charter for the International Trade Organization (ITO) as Article 38 and also as Article X of the GATT, which survived the demise of the ITO and has remained effective in current WTO trading rules.[88]

The Uruguay Round did not change the text of Article X from what had been initially adopted in 1947. What did change was the shift in focus of the GATT from border measures, such as tariffs and quotas, to non-tariff barriers such as technical safety and environmental regulations. The elimination of non-tariff barriers is not controlled by borders, but instead depends on domestic regulatory procedures. Thus, transparency, as an important element

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83 Abram Chayes, 1998, p. 43.

84 Sylvia Ostry, 'China and the WTO: The Transparency Issue', 1998.

85 Padideh Ala'I, 'The Multilateral Trading System and Transparency', in Alan S. Alexandroff (ed.), *Trends in World Trade – Essays in Honor of Sylvia Ostry*, Carolina Academic Press, 2007, p. 107; Sylvia Ostry, 'External Transparency: the Policy Process at the National Level of the Two-level Game', in Mike Moore (ed.), *Doha and Beyond: The Future of the Multilateral Trading System*, Cambridge University Press, 2004, p. 112.

86 Sylvia Ostry, 'China and the WTO: The Transparency Issue', 1998.

87 US Dept. of State, Suggested Charter for an International Trade Organization of the United Nations, 1946. Sylvia Ostry, 'China and the WTO: The Transparency Issue',1998.

88 Sylvia Ostry, 'China and the WTO: The Transparency Issue',1998.

in good governance and effectiveness of the administrative regime, has been adopted in the texts of many WTO covered agreements, including the TBT Agreement,[89] SPS Agreement,[90] Import Licensing Agreement,[91] Agreement on Safeguards,[92] Anti-dumping Agreement,[93] Agreement on Government Procurement,[94] and the SCM Agreement[95]. The TBT and SPS Agreements, for example, not only require publication of the standards ultimately adopted, but also provision of a reasoned explanation and an *a priori* opportunity for foreign governments to comment and discuss the proposed standards.[96]

Similar provisions are also found in the GATS and Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Article III of the GATS and Article 63 of TRIPS are entitled 'Transparency' and largely follow the provisions of Article X:1. In addition, for example, to the publication requirement, Article III of the GATS requires WTO members annually to inform the WTO Council for Trade in Services of any changes in laws that affect trade in services.[97] It also requires members to establish one or more enquiry points for providing specific information to other members.[98]

There are multiple references to transparency in the legal framework of the WTO.[99] Provisions explicitly or implicitly referring to the term 'transparency' are closely linked to provisions on notification obligations. In addition to the provisions in the agreements, WTO also includes an important tool, the Trade Policy Review Mechanism (TPRM), which aims to enhance transparency and which subjects trade and related policies to a periodic review in order to ensure significantly greater transparency in national policies.[100]

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89 Agreement on Technical Barriers to Trade, Articles 2.9-2.12 (notification and publication), Article 10 (enquiry points).

90 Agreement on Sanitary and Phytosanitary Measures, Article 7 & Annex B (publication, enquiry points and notification).

91 Agreement on Import Licensing Procedures, Articles 1.4 and 3.3 (publication).

92 Article 3.1 (publication).

93 Agreement on Implementation of Article VI of GATT 1994, Article 12.

94 The preamble of the Agreement on Governmental Procurement states that parties to this agreement recognize that it is desirable to provide transparency to laws, regulations, procedures and practices regarding to governmental procurement. Many transparency requirements, including publication and notification, are provided fin this agreement, including Articles V.11 and VIII (a).

95 Agreement on Subsidies and Countervailing Measures, Article 22 (public notice).

96 Carl-Sebastian Zoellner, 'Transparency: An Analysis of an Evolving Fundamental Principle in International Economic Law', Michigan Journal of International Law, vol. 27, 2006, p. 592.

97 GATS, Article III 3.

98 GATS, Article III 4.

99 Friedl Weiss, assisted by Silke Steiner, 'Transparency as an Element of Good Governance in the Practice of the EU and the WTO: Overview and Comparison', *Fordham International Law Journal*, vol. 30, 2007, p. 1579.

100 Friedl Weiss, 2007, p. 1583.

### *2.2.1.2 Enforcement of GATT Article X:1*

Imposing transparency obligation on members' domestic regulatory regime has been a challenging task for the WTO as it has had to seek to maintain a balance between two conflicting interests: on the one hand, this obligation is essential for the effectiveness of trading rules, while on the other hand it may undermine members' exercising of their sovereignty. The intrusive nature of the transparency requirement has also created specific difficulties for the DSB in seeking to enforce this obligation. Essentially, enforcement involves two aspects.

1. The DSB has been reluctant to rule on Article X:1 or to apply it strictly. The publication requirement provided for in Article X:1 GATT, which is described as one of the most positive but least known features of WTO law,[101] has received relatively little attention.[102] Dispute settlement proceedings demonstrate that the DSB was initially very reluctant to rule on this Article. While frequently cited in complaints and DSB rulings, violations of Article X have typically been presented merely as 'add-ons' to other, more promising claims of violations of the WTO rules.[103] WTO and GATT panels have habitually refused to rule on Article X claims where a measure has already been found to violate another, more substantive GATT or WTO obligation.[104] Claims under Article X have tended to be regarded merely as subsidiary matters. In *Indonesia – Autos*, for example, the Panel had to examine whether measures taken by Indonesia to develop its domestic automobile industry were inconsistent with Article X, as well as with Articles I and III GATT.[105] However, once the Panel found that Indonesia had violated the provisions of Article I and/or Article III of GATT, it considered it unnecessary to examine the claims under Article X GATT.[106]

In many WTO cases, there has been a concerted attempt to rule on the applicability of Article X, and the claims that it had been violated were not dismissed as subsidiary matters.[107] However, the Panel and the Appellate Body (AB) seem to have adopted a very restricted approach to interpreting the scope of Article X, thus making it difficult to find that it had

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101 According to Steve Charnovitz, one of the most positive but least known features of WTO law is the rule requiring national governments to publish laws, regulations, judicial decisions, and administrative rulings affecting trade. Steve Charnovitz, 'The WTO and Cosmopolitics', *Journal of International Economic Law*, vol. 7, 2004, pp. 675 & 678. Friedl Weiss, 2007, p. 1572.

102 Robert Howse, 'How to Begin to Think about the Democratic Deficit in the WTO, in Stefan Griller (ed.), *International Economic Governance and Non-Economic Concerns*, Springer, 2003, p. 91. Friedl Weiss, 2007, p. 1573.

103 Friedl Weiss, 2007, p. 1573.

104 Warren Maruyama, 2003, p. 677.

105 Report of the Panel, Indonesia – Certain Measures Affecting the Automobile Industry, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, 2 July 1998.

106 Report of the Panel, Indonesia – Certain Measures Affecting the Automobile Industry, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, 2 July 1998. Friedl Weiss, 2007, p. 1574.

107 Padideh Ala'i, 2007, p. 123.

been violated.[108] There have been relatively few interpretations made under Article X:1 in respect of the publication requirements, except the one made on its 'general application'. Article X:1 requires publication of all trade-related laws, regulations, and administrative ruling of 'general application'. The AB has stated that, for a measure to be within the scope of Article X, it must be of 'general application' and that administration of a measure in a 'specific case' is not within its scope.[109] In *EC – Importation of Certain Poultry Products*, Brazil objected to the application of quotas on imports of poultry by the EC and argued that it was a violation of Article X if traders did not know upon arrival whether a particular shipment would be subject to in-quota or out-of-quota trade rules.[110] The AB held that the scope of Article X was limited to measures of general application and that licenses issued to a specific company or applied to a specific shipment were not measures of general application.[111]

The Panel's ruling in *Japan – Customer Photographic Film and Paper* also demonstrated another difficulty as regards the 'burden of proof' in establishing violations of Article X:1. The US argued that the government of Japan had operated under a 'shield of opacity' in undertaking a concerted and coordinated program to replace formal tariff and investment restrictions with regulatory and structural barriers that would be less identifiable as inconsistent with Japan's international obligations.[112] Although *Japan – Customer Photographic Film and Paper* was not a violation case and US did not claim a violation of Article X, transparency was central to the claim of the US and the Panel did discuss Article X.[113] The Panel held that Article X 'applied to administrative rulings in individual cases if such rulings establish or revise principles or criteria applicable in future cases'.[114] But, in that case, the US had failed to 'clearly demonstrate the existence of such unpublished administrative rulings in individual matters'.[115] The Panel's analysis is circular to the extent that it is always difficult to prove the existence of an unpublished administrative ruling if it is unpublished, non-transparent and 'shrouded in secrecy'.[116] After acknowledging this problem, the Panel

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108 Padideh Ala'i, 2007, p. 129.

109 WTO Analytical Index – Guide to WTO Law and Practice, World Trade Organization, 2003.

110 Report of the Appellate Body on European Communities – Measures Affecting the Importation of Certain Poultry Products, July 13, 1998, WT/DS69/AB/R, paras. 115-116.

111 Report of the Appellate Body on European Communities – Measures Affecting the Importation of Certain Poultry Products, July 13, 1998, WT/DS69/AB/R, para. 102. Padideh Ala'i, 2007, p. 128.

112 Report of the Panel on Japan – Measures Affecting Consumer Photographic Film and Paper, paras. 7.2, 10.22-10.24, 31 March 1998, WT/DS44/R. Padideh Ala'i, 2007, p. 128.

113 Padideh Ala'i, 2007, p. 128.

114 Report of the Panel on Japan – Measures Affecting Consumer Photographic Film and Paper, para. 10.388.

115 Report of the Panel on Japan – Measures Affecting Consumer Photographic Film and Paper, para. 10.388.

116 Report of the Panel on Japan – Measures Affecting Consumer Photographic Film and Paper, para. 10.390. The Panel acknowledged this reality as follows: 'We acknowledge that the nature of the US claim makes it difficult to cite examples – if a ruling is unpublished how can the United States know that it effects such changes?', Padideh Ala'i, 2007, 128.

still maintained that the US had failed to 'cite examples of changed policies that it believes were in fact implemented first in unpublished decisions'.[117]

2. The AB's interpretation of this Article was inconsistent. In *US – Import of Carbon Quality Line Pipe*, the Panel ruled that the US had violated the transparency requirements in Articles 3.1 and 4.2 (c) of the Agreement on Safeguards[118] by failing to publish a report on the application of the safeguard that included a finding or reasoned conclusion.[119] However, the AB reversed the Panel's determination[120] by stating that:

> We are not concerned with *how* the competent authorities of WTO Members reach their determinations in applying safeguard measures. The Agreement on Safeguards does not prescribe the internal decision-making process for making such a determination. That is entirely up to WTO Members in the exercise of their sovereignty. We are concerned only with the *determination itself*, which is a singular act for which a WTO Member may be accountable in WTO dispute settlement.[121]

Although these rulings were not made in connection with Article X, the AB's reluctance to delve into the internal decision-making process of a member may explain its attitude to the general transparency requirement reflected in Article X.[122] The statement that the internal decision-making process is outside the WTO's competence, but falls entirely within a member's sovereignty is at odds with the spirit of Article X, as well as with the AB's ruling in an earlier case. In fact, the AB recognized the spirit of Article X in the *Shrimp* case,[123]

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117 Report of the Panel on Japan – Measures Affecting Consumer Photographic Film and Paper, para. 10.393, Padideh Ala'i, 2007, p. 128.

118 Article 3.1 of the Agreement on Safeguards provides that 'A Member may apply a safeguard measure only following an investigation by the competent authorities of that Member pursuant to procedures previously established and made public in consonance with Article X of GATT 1994. This investigation shall include reasonable public notice to all interested parties and public hearings or other appropriate means in which importers, exporters and other interested parties could present evidence and their views, including the opportunity to respond to the presentations of other parties and to submit their views, *inter alia*, as to whether or not the application of a safeguard measure would be in the public interest. The competent authorities shall publish a report setting forth their findings and reasoned conclusions reached on all pertinent issues of fact and law.' Article 4.2 (c) provides that 'The competent authorities shall publish promptly, in accordance with the provisions of Article 3, a detailed analysis of the case under investigation as well as a demonstration of the relevance of the factors examined.'

119 Panel Report on United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea, October 29, 2001, WT/DS202/R, para. 8.1 (3).

120 Report of the Appellate Body on United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea, WT/DS202/AB/R, February 15, 2002, para. 263 (d).

121 Report of the Appellate Body on United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea, WT/DS202/AB/R, February 15, 2002, para. 158.

122 Padideh Ala'i, 2007, p. 130.

123 United States – Import Prohibition of Certain Shrimp and Shrimp Products, Panel report was adopted on 15 May 1998.

in which it ruled that although the measure itself was permitted under Article XX (g), it had been applied in an arbitrary and discriminatory manner in violation of the preamble of Article XX.[124] In its ruling it stated that:

> Article X:3 of GATT 1994 establishes certain minimum standards for transparency and procedural fairness in the administration of trade regulation which, in our view, are not met here. The non-transparency and *ex-parte* nature of the internal governmental procedures applied by the competent officials…are all contrary to the *spirit*, if not the letter, of Article X:3 of GATT 1994.[125]

The AB seems to have adopted an indeterminate approach to interpreting the transparency requirement. There may be competing interests and concerns behind this.[126] On one hand, the AB recognized that, as a general rule, lack of transparency poses a serious challenge to the market access goals of the multilateral trading system.[127] On the other hand, it deemed that evaluating the functioning of internal administrative policies of members, as expressed in Article X, could be an unacceptable infringement of members' sovereignty.[128] The competing concerns are also reflected in the restricted provisions on domestic transparency. Annex 3 of the Agreement Establishing the World Trade Organization on Trade Policy Review Mechanism contains the provisions on 'domestic transparency':

B. Domestic transparency

> Members recognize the inherent value of domestic transparency of government decision-making on trade policy matters for both members' economies and the multilateral trading system, and agree to encourage and promote greater transparency within their own systems, acknowledging that the implementation of domestic transparency must be on a *voluntary basis* and take account of each member's legal and political system.[129]

This definition of transparency goes to the heart of a country's legal infrastructure, while also connecting with various political and social values, and more specifically to the nature and enforcement of its administrative legal regime. For fear of undermining the legitimacy of the multilateral trading system, the WTO, as well as the AB, is reluctant to establish substantive standards on transparency to be enforced in all member states that may have conflicting

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124 Report of the Appellate Body on United States – Import Prohibition of Certain Shrimp and Shrimp Products, 12 October 1998, WT/DS58/AB/R, paras. 181-184.

125 Report of the Appellate Body on United States – Import Prohibition of Certain Shrimp and Shrimp Products, 12 October 1998, WT/DS58/AB/R, para. 183.

126 Padideh Ala'i, 2007, p. 130.

127 Padideh Ala'i, 2007, p. 130.

128 Padideh Ala'i, 2007, p. 130.

129 The Result of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts, p. 434. Article B, Trade Review Mechanism, Annex 3 of the Agreement Establishing the World Trade Organization.

or at least distinct administrative legal systems and political and social values. Thus, a set of procedural requirements, represented by Article X, has been established in various WTO agreements to ensure a minimum degree of transparency. The lack of substantive standards may, however, bring about difficulties in the enforcement of transparency obligations. Article 5 (1) of the Agreement on Trade-Related Investment Measures states, for example, that 'Members shall notify the Council for Trade in Goods of all trade-related investment measures they are applying that are not in conformity with the provisions of this Agreement'. This provision is only a general obligation and does not set any standards against which violations of this Article can be determined.

In summary, the transparency obligations in the WTO agreements are drafted restrictedly, setting minimum standards for domestic transparency through procedural requirements. The enforcement and practice of Article X GATT in dispute settlement proceedings remains limited. Article X GATT rarely plays a central role in cases before the WTO,[130] and the DSB tends to interpret it narrowly, thus making it difficult for members to successfully assert violations of Article X.

### 2.2.2 China's WTO-plus Obligations on Transparency

Foreign traders and investors have complained about the lack of transparency in China for years. The large size and diversity of the country, and its unique legal system, have often made it difficult for foreign businesses to establish the rules applying in any given situation.[131] The Protocol on the Accession of People's Republic of China (Accession Protocol) includes a separate section on 'transparency' under the heading of 'Administration of Trade Regime'.[132] The transparency commitments provided in the Accession Protocol are based on, but go beyond the requirements specified in Article X GATT. By expanding the scope of the normal WTO transparency requirements, the Accession Protocol creates a greater burden for China than for other WTO members and has thus led some to describe the requirements as 'WTO-plus'.[133]

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130 The first case in which Article X GATT played a central role is that of *European Communities – Selected Customs Matters*, WT/DS315/R, 16 June 2006. The rulings in this case focused on Article X:3 and will thus be discussed in Chapters IV and V. See Friedl Weiss, assisted by Silke Steiner, 'Transparency as an Element of Good Governance in the Practice of the EU and the WTO: Overview and Comparison', *Fordham International Law Journal*, vol. 30, 2007, p. 1574.

131 Julia Ya Qin, 'WTO-Plus Obligation and Their Implication', 2003, pp. 483-522.

132 Accession Protocol, Part I 2 (c).

133 Julia Ya Qin, 'WTO-Plus Obligation and Their Implication', 2003, pp. 483-522; Roy A. Schotland, 'Tracking Transparency: An American Administrative Lawyer Stumbles into WTO-land', Georgetown University Law Center, Speech in Shanghai, China, February 2001. See also Christopher Duncan, 'Out of Conformity, China's Capacity to Implement World Trade Organization Dispute Settlement Body Decisions after Accession', *American University International Law Review*, 2002.

There are four main aspects in China's WTO-plus obligations on transparency. The first relates to the publication requirement, which expands the scope of the publication requirement in Article X to include all laws, regulations and other measures in trade in goods, services, TRIPS and the control of foreign exchange.[134] This means that China must make all laws, regulations and other measure readily available to other WTO members requesting information.[135] Moreover, all laws, regulations and other measures affecting trade in any area require publication before they can be enforced.[136] By contrast, Article X restricts this requirement to measures resulting in an advance in a rate of duty or imposing a new or more burdensome barrier on imports.[137]

The second aspect relates to the requirement for an enquiry point, which goes beyond the scope of Article X. It requires China to establish a single enquiry point, where any individual, enterprise or WTO member may request all information concerning Chinese laws, regulations and other measures within the mandate of the WTO. China must respond to requests within thirty days of receiving them or, in exceptional circumstances, within forty-five days. Since many other WTO members do not have a single enquiry point for information, imposing the enquiry point requirement on China appears excessive.[138] It raises doubts about China's ability to fulfill this requirement because domestically China does not have a single enquiry point that can provide a comprehensive account of all Chinese legislation. Some believe that while enquiry points are essential to the distribution of relevant information, the WTO must be realistic as to how much or little authority responses from such an enquiry point can have,[139] especially when a country, such as China, is plagued by poor governmental and legal structures.[140]

The third aspect concerns the requirement for the right to comment, which also goes beyond the scope of Article X. China is required to allow a reasonable period for comments to be submitted to the appropriate authorities before such measures are implemented. The Accession Protocol allows an exception for laws, regulations and other measures involving national security, specific measures setting foreign exchange rates or monetary policies, and other measures where publication would impede law enforcement. The comment requirement is the most intricate and intrusive transparency commitment that the Accession Protocol imposes on China. It is modeled on the US Administrative Procedure Act,[141] which US scholars describe as 'one of the most important advances in modern democracy', resulting from the requirement's positive impact on the promulgation of comprehensive laws and

134 Accession Protocol, Part I Article 2 (C), para. 2.
135 Accession Protocol, Part I Article 2 (C), para. 1.
136 Accession Protocol, Part I Article 2 (C), para. 1.
137 GATT, Article X:2.
138 Christopher Duncan, 2002.
139 Roy A. Schotland, 2001.
140 Christopher Duncan, 2002.
141 Sylvia Ostry, 'China and the WTO: The Transparency Issue',1998.

regulations.[142] 'Right to comment' has been deemed to be the most problematic area in China's transparency responsibilities since China has not yet introduced a requirement, in the form of legislation, for mandatory public consultation during the drafting process of laws.

The final aspect relates to the special Transitional Review Mechanism (TRM) established for China. The TPRM was created by the WTO to increase the transparency and understanding of members' trade policies and practices through regular monitoring. A special TRM, which differs from the normal TPRM, was included in China's accession agreements.[143] Under this mechanism, the subsidiary bodies with a mandate covering China's commitments under the WTO agreements or the Accession Protocol have to review China's implementation, as does the General Council. Both the review by the subsidiary bodies and that by the General Council have to be conducted annually for the first eight years after the country's accession, followed by a final review in the tenth year or at an earlier date decided by the General Council. It should be noted that this review mechanism supplements rather than supplants the normal committee review and TPRM.[144] That is to say, in addition to the annual review by subsidiary bodies and the General Council, China will be subject to a regular TPRM every four years, depending on its share of current world trade.

The TRM has two special features that differ from the TPRM. First, the scope of the review and the WTO bodies involved are much wider than the normal trade review.[145] It involves sixteen subsidiary bodies of the WTO, each with a responsibility for China's commitments in the area of that body's mandate.[146] By contrast, the TPRM is conducted by the Trade Policies Review Body and does not involve so many subsidiary bodies or a higher level of the General Council's comprehensive review.[147] This latter review covers virtually all the important aspects of China's economic and trade policies and practices, including economic data, economic policies, the framework for making and enforcing policies, and policies affecting trade in goods, services and intellectual property rights. The annual review by the General Council has to be conducted in accordance with the results of reviews by the subsidiary bodies. In addition, it includes an examination of the development of China's trade with WTO members and other trading partners, and recent developments and cross-sectoral issues regarding China's trade regime. Second, this review is intended to be more intrusive in that it aims to evaluate not only the general economic and trade policies, but also the specific progress achieved in implementing the WTO agreements, including progress achieved in

142 Christopher Duncan, 2002.

143 Accession Protocol, Part I 18.

144 Xin Zhang, 'Implementation of the WTO Agreements: Framework and Reform', *Northwestern Journal of International Law and Business*, Winter, 2003.

145 Xin Zhang, 2003.

146 Xin Zhang, 2003.

147 Xin Zhang, 2003.

withdrawing or amending inconsistent legislation and so on.[148] The latter requirement is beyond the scope of TPRM.[149]

The country-specific WTO-plus obligations imposed on China may reflect trading partners' main concerns about China's poor performance on transparency. WTO's normal requirements may not be enough to enhance China's low transparency level compared to that of many other members, and thus the WTO-plus obligations can plug the gap whenever the normal WTO rules are not working. Another possible explanation is that a higher level of transparency commitments may ensure that a WTO-satisfactory level of transparency is still achieved even if China is not fully compliant with those commitments. There are two primary reasons, however, why those WTO-plus obligations on transparency are difficult to justify. Firstly, it is not rational or realistic to require a weaker member to comply with stricter commitments. Secondly, the WTO seems to have adopted a contradictory approach on compliance with this requirement: on the one hand, the DSB is generally reluctant to enforce this requirement strictly, while on the other hand, in the specific case of China, the WTO has imposed stricter requirements that go beyond the WTO provisions. In spite of the lack of rationality in the WTO-plus obligations, the important question is whether this approach will help improve China's weak performance on transparency. More specifically, will the stricter requirement necessarily be more effective in correcting poor performance, and how may the DSB's indeterminate attitude on enforcement of this Article affect China's compliance? The study in the following sections of the obstacles to transparency, which are deeply rooted in China's regulatory regime, sheds some light on answers to these questions.

## 2.3 GENERAL OBSTACLES TO TRANSPARENCY IN CHINA'S LEGISLATIVE REGIME

As discussed above, the transparency requirement in the WTO agreement goes to the heart of a member's legal and administrative system. The transparency of trade-related laws, regulations and legal measures does not exist in isolation. Rather, it is closely connected to the characteristics of the legal and administrative system in general. Since China's legislative regime has been developed without regard to the transparency principle, the real challenge for China in seeking to comply with this requirement goes beyond what is required in Article X:1. In fact, many non-transparency practices in the country's foreign trade regime result from its problematic legislative regime and non-transparent administration of rules at the local level.

148 Xin Zhang, 2003.

149 Xin Zhang, 2003.

### 2.3.1 Brief Introduction of Governmental Structure and Distribution of Legislative Power

In order to understand the opaqueness of the regulatory regime in China, the basic state structure upon which the legislative organs have been built first has to be explained. Unlike the Western state structure, which is characterized by separation of the three powers, China's basic political system is theoretically based on the system of the People's Congress. The relationship between judicial, prosecutorial and administrative bodies is neither parallel nor subject to mutual restriction and supervision. These bodies' powers are vested in the National People's Congress (NPC), to which they are responsible and to which they report their work. The NPC is the highest organ of state power, with the Standing Committee as its permanent body. According to China's Constitution, the NPC and its Standing Committee exercise the legislative power of the state.[150] The NPC exercises its legislative power in amending the Constitution, supervising the enforcement of the Constitution, and enacting and amending basic laws and statues governing criminal offenses, civil affairs, state organs and other matters.[151] The Standing Committee of the NPC is entitled to interpret the Constitution and supervise its enforcement; to interpret laws; to enact and amend laws with the exception of those to be enacted by the NPC; to annul administrative rules and regulations, decisions or orders of the State Council that contravene the Constitution or laws, and to annul those regulations or decisions of the provincial organs of state power that contravene the Constitution, laws or the administrative regulations of the State Council. The NPC also has the power to elect the country's president and vice president.

The State Council, which is the highest administrative organ of the state, is entitled to issue administrative regulations and to issue decisions and orders that are in accordance with the Constitution and laws.[152] It is composed of a Premier, Ministers in charge of ministries and Commissioners in charge of commissions. The Premier of the State Council is elected by the NPC, based on the nomination by the President. The State Council has the power to alter or annul inappropriate directives, orders or regulations issued by ministries and commissions, or directives and orders issued by local organs at different levels. The Supreme People's Court and Supreme People's Procuratorate exercise the highest judicial power and the highest prosecutorial power respectively of the state. Both of them are responsible to the NPC.[153] The President of the Supreme People's Court and the Procurator-General of the Supreme People's Procuratorate are elected by the NPC.[154]

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150 Article 58 of the Constitution of the People's Republic of China, promulgated in 1982, amended in 1999.

151 Article 62 (1), (2) and (3) of the Constitution of the People's Republic of China, promulgated in 1982, amended in 1999.

152 Article 85 and 89 of Constitution of People's Republic of China, promulgated in 1982, amended in 1999.

153 Article 128 and Article 133 of Constitution of People's Republic of China, promulgated in 1982, amended in 1999.

154 Article 62 (7) and (8) of Constitution of People's Republic of China, promulgated in 1982, amended in 1999.

Similar terms apply to the structure of state power at the local levels. People's congresses and people's governments are established at various local levels, such as provinces, cities, counties and towns. Local people's congresses are the local organs of state power, and local governments exercise executive functions. Local people's congresses and local governments all have powers to issue local decrees and rules in accordance with laws and the needs of local areas. However, decrees issued by local people's congresses are superior to rules issued by local governments. The local people's congress at a provincial level may enact local decrees, provided they do not contravene any provision of the Constitution, national laws or administrative regulations of the State Council. Local people's congresses in major cities may also adopt local decrees, provided they are not incompatible with those enacted by people's congresses in provinces where the major cities are located. Local governments also enjoy the right to issues local rules, provided they do not contradict national laws, administrative regulations of the State Council or local decrees of the local people's congresses. Thus, as the representation of the highest state power, laws or regulations enacted by the people's congress will in principle always prevail over those enacted by governments at the same administrative level. The state power structures at both central and local levels are shown in following tables.

**Table 1: Structure of State Power in China**

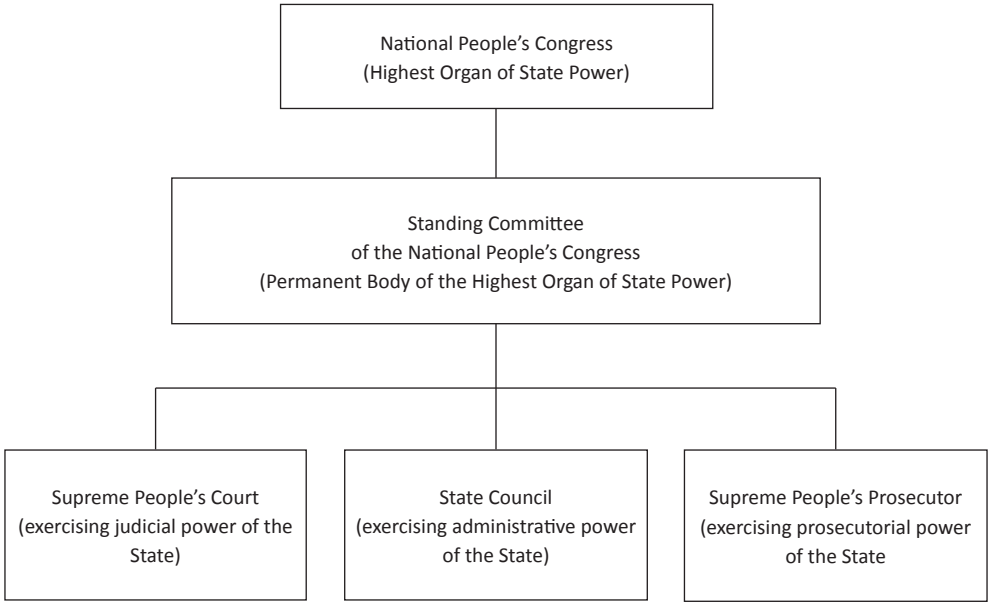
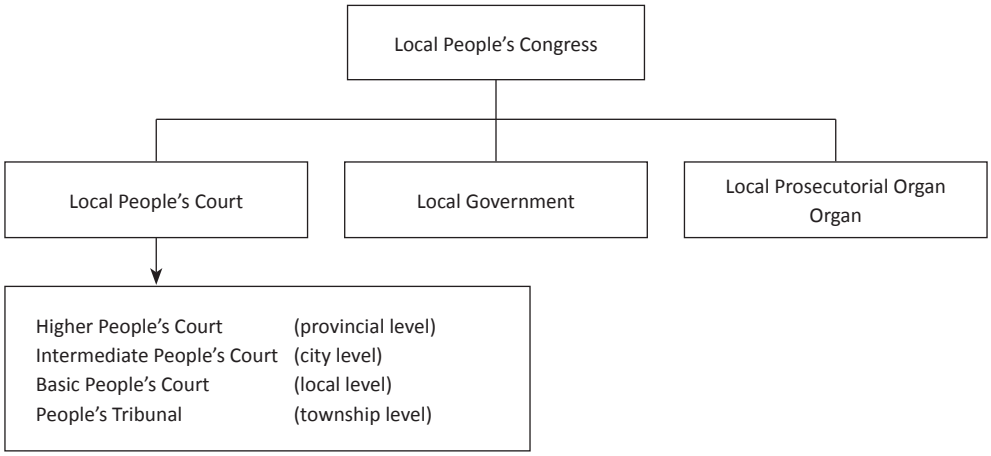


**Table 2: The Structure of State Power at Local / Provincial Level**




## 2.3.2 Problems in Legislative Regime

At the risk of oversimplifying, it could be stated that a five-tier legal system has been established in accordance with the provisions in the Constitution and the Legislative Law.[155] The hierarchy of this five-tier legal system can essentially be summarized as follows.

**Table 3: Hierarchy of Five-tier Legal System**

Constitution
– National People's Congress
↓
Laws/Statutes
– National People's Congress
↓
Administrative Regulations
– State Council
↓
Local Decrees
– Local People's Congress (provincial level > city level)
↓
Rules
(Local Rules & Ministerial Rules) -- Local Governments & Ministries and Departments under the State Council

155 The Legislative Law of the People's Republic of China was issued by the NPC in 2000.

Although the distribution of legislative powers and the hierarchy of legislative enactments seem clear, the real situation is much more complicated.

#### *2.3.2.1 Diffusion of Rulemaking Powers and Conflicting Legal Authority*

In China, the legislative and administrative governmental bodies both have the power to issue legislative documents. In addition to the people's congresses at both national and local levels, which are constitutionally regarded as legislative organs of state, many other administrative entities have the right to legislate. As the above table demonstrates, ministries, commissions, and departments under the State Council, as well as the government and administrative organs at various local levels all enjoy the right to issue legal texts with varying degrees of legal force.

At the central level, the hierarchy of the Constitution, laws and statutes, and the administrative regulations of the State Council is comparatively clear, and all of them are superior to legislation enacted at local levels. At the local level, by contrast, the relationship between local decrees and rules is quite confusing. 'Local decrees' are decrees or regulations enacted by provincial people's congresses or people's congresses in major cities.[156] The local decrees enacted by the former are superior to those enacted by the latter. 'Rules' are 'local rules' issued by local governments and 'ministerial rules' issued by ministries, commissions or departments under the State Council. As explicitly provided for in the Legislative Law, 'local decrees' are superior to 'local rules' issued by the government at the same or a lower administrative level, while the legal authority of 'local rules' is equal to 'ministerial rules'.[157] According to this formula, 'local decrees' should be higher than 'ministerial rules'. However, there are some confusing provisions as regards to the legal authority level of 'ministerial rules' in the Legislative Law, implying that 'local decrees' are on the same legal authority level as 'ministerial rules'. Firstly, Article 80 of the Legislative Law provides that 'local decrees' are superior only to 'local rules', rather than to 'rules' in general. It excludes 'ministerial rules' from those that are inferior to 'local decrees'. It implies that 'ministerial rules' are probably at the same level with 'local decrees'. Secondly, Article 86 (2) of the Legislative Law explicitly states that if there is a conflict between 'ministerial rules' and 'local decrees', the competent authorities will decide which shall prevail. It again implies that 'ministerial rules' are at the same level as 'local decrees'. The confusing and interwoven provisions of legislative enactments and their legal authorities make legislation quite complex and confusing. The situation will be even more complicated in the event of a conflict between legal texts with the same level of legal authority, but issued by different parallel administrative organs.

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156 'Major cities', adopted in Legislative Law, refer to provincial capitals, special economic zones and other major cities approved by the State Council. See Article 63 of Legislative Law.

157 Articles 80 and 82 of Legislative Law.

Conflicting Provisions in the Legislative Law Article 80-86 as regards to Legal Authority Level

| |
|---|
| Local Decrees > Local Rules |
| Local Rules = Ministerial Rules |
| Local Decrees = Ministerial Rules |

### *2.3.2.2 Miscellaneous Formats of Legislation*

As explained by Lubman, the allocation of rulemaking powers by agencies within the Chinese bureaucracy is a major structural problem in the organization of the state.[158] Much legislative power has been delegated to the provincial level, with more than twenty functional bureaucracies for the central government. The State Council supervises more than sixty departments (including ministries), commissions, administrations and offices. These agencies are authorized to issue rules to implement specific legislation under powers granted by a legislative body such as the Standing Committee of the NPC. Their authority also stems from a general rulemaking power that is deemed to be inherent in the agencies and enables them to issue any rule that is necessary to carry out their tasks.[159]

Miscellaneous formats of legislative enactments have been adopted by administrative rulemaking bodies. Besides the 'administrative regulations' or 'ministerial rules', which are clearly regulated and provided for in the Legislative Law, the State Council and its sub-authorities may also enact or issue administrative measures, provisions, directives, decisions, orders, notices, explanations and so forth, all of which are claimed to be normatively binding and treated as such by the creating entities. In contrast to laws and regulations, which are normally drafted with great flexibility and in broad and general language, these less 'formal' but more detailed administrative rules are more frequently used by administrators in various provisional circumstances and are subject to less supervision. The large quantity of these legal documents increases the difficulty of publication and public accessibility in all cases. Indeed, lawyers and officials in China engage in a daily struggle to make sense of vague, inconsistent laws and often questionable legislative authorities.[160]

In summary, the chronic disorder in Chinese legislation, composed of interwoven provisions and conflicting legal authority, is a defining feature in the opacity of Chinese legislative enactments. As Keller commented, 'The disparate mass of laws and regulations which makes up the formal written sources of Chinese law does not possess sufficient unity to

158 Stanley Lubman, 'Bird in a Cage: Chinese Law Reform after Twenty Years', *Journal of International Law & Business,* Spring 2000.

159 Stanley Lubman, 'Bird in a Cage', 2000.

160 Perry Keller, 'Sources of Order in Chinese Law', *American Journal of Comparative Law*, vol. 42, No. 4, Autumn 1994

be regarded as a coherent body of law. In their disarray, the sources of Chinese law seem barely capable of providing the basic point of reference which all complex systems of law require'.[161]

## 2.4 OBSTACLES TO PUBLICATION REQUIREMENT DUE TO EXISTENCE OF INFORMAL LAWS

The above discussion demonstrates that the opaque legal regime in China may be partially attributed to problems embedded in the law-making process, including an unclearly defined hierarchy, conflicting legal provisions issued by authorities at the same administrative level, and excessively complicated formats of formal and informal legislation. Whether, once issued, legislation can be publicly assessed is another critical factor defining the transparency of China's legal system. While the laws and regulations at the central level are normally published in accordance with the Legislative Law requirements, the rules at the local level, especially those issued by local administrative authorities, constitute a major problem.

### 2.4.1 Publications Requirements scattered across Laws and Regulations

The Legislative Law is the first law governing the rulemaking process and legislative agencies. It standardizes the basic transparency requirements for rulemaking. Articles 52 and 62 require that, upon promulgation, laws enacted by the NPC and administrative regulations of the State Council must be published in a timely manner in the Bulletin of the NPC Standing Committee, the State Council Bulletin, and in nationally circulated newspapers. In the case of local decrees, publication is required in a timely manner in the Bulletin of the Standing Committee of the people's congress in that region and the newspaper circulating within that jurisdiction.[162] Local rules are also required to be published in the local government Bulletin and a newspaper circulated in the local jurisdiction.[163] More publication requirements can be found in other laws and administrative regulations, such as the Price Law, the Administrative Punishment Law, the Regulation of Procedures Adopting Administrative Regulations and so on.

Besides the legal provisions, some other legal mechanisms – for instance, the system of hearings – have also preliminarily been established to improve transparency. Normally there are three kinds of hearings: a legislative hearing, the hearing of administrative decision and the hearing of specific administrative actions. The hearing of specific administrative actions is better developed than the other two kinds of hearings. This is reflected in the

161 Perry Keller, 1994.

162 Article 70 of the Legislative Law of People's Republic of China.

163 Article 77 para.2 of the Legislative Law of People's Republic of China.

Administrative Punishment Law, which includes a separate section on 'public hearings'.[164] With regard to legislative hearings, the Legislative Law contains only some general provisions, which provide that 'in the process of drafting an administrative regulation, the drafting body shall gather opinions from a wide circle of constituents such as the relevant agencies, organizations and citizens. The gathering of opinions may be in various forms such as panel discussion, feasibility study meeting, hearing etc'.[165]

However, these scattered legal provisions and mechanisms are far from sufficient to be regarded as a unified and effective principle guiding the publication of legislation. Publication requirements imposed on the enactment of laws, regulations, local decrees and rules remain very simple and general. There is no stipulation that only those laws, regulations and so on that have been published can be enforced, and no time limit for publication after promulgation has been set. Moreover, the major transparency requirements provided in the Legislative Law are not applicable to 'normative documents' issued extensively by local administrative authorities, and this may constitute a key obstacle to a transparent legal and administrative regime in China.

### 2.4.2 Adoption of 'Normative Documents'

In addition to formal Chinese legislation (laws, administrative regulations, local decrees and rules), there is another body of 'rules' that plays a significant role in the regulatory regime. These 'normative documents' are used extensively by administrative bodies, especially at local levels. They may take many forms, such as decisions, notices and provisions, and they have general binding force on all activities.

The normative documents are a relic of the pre-reform period, when legal mechanisms were largely absent.[166] Although the progress achieved in improving Chinese legal infrastructure makes normative documents much less of a problem today, these documents continue to exist in all areas at various local levels. The legality of the normative documents is unclear under current Chinese law. Basically, they are not covered by the regulation governing legislative procedures and formats in China. The Legislative Law and other relevant national regulations on rulemaking are silent on the existence of normative documents, and thus the publication requirements provided for in the Legislative Law do not apply to these documents. In practice, internal decisions or notices may never be made known to the general public, but nevertheless have binding force of law. In some cases, they are published

164 Articles 42 and 43 of the Administrative Punishment Law, issued on 17 March 1996.

165 Article 58 of the Legislative Law of People's Republic of China.

166 Sylvia Ostry, 'China and the WTO: The Transparency Issue', 1998.

only in obscure local newspapers, thus making it virtually impossible for anyone to know exactly which rules apply.[167]

Case Study[168]

Normally, the application fee for an auto import license in Hainan province is 10 yuan under the local government's regulation. In September 2002, however, the auto importers in Hainan province received an 'oral notice' from the local 'Electromechanical Products Office', which is the administrative authority for imports and exports of electromechanical products in Hainan province. This oral notice stated that 'extra fees will be charged for auto import licenses: 40,000 yuan for normal cars, 30,000 for cross-country cars and 20,000 for vans'. This charge was much higher than the standard. Two month later, in November 2002, the charging of the extra fee was officially explained as the collection of a 'foreign trade development fund', and an 'official document' or 'normative document' was accordingly issued to make this charge legally binding. This 'normative document' was jointly issued by the Department of Commerce and the Department of Finance of Hainan province on 27 August 2003, with the result that the 'foreign trade development fund' was set up by the government to support exports and one of its three sources of income was earnings from bidding for or compensable use of import and export quota licenses. The character of the 'normative document' adopted in this case could be categorized as follows: (1) it was issued by departments under the provincial government and had general binding force for all auto import license application in Hainan province; (2) it was not compatible with general regulations on this issue and specifically contradicted a rule issued by the central authority that prohibited local authorities from abusing their rights to make profits on the issuance of import licenses; (3) its provisions were vague and included some disguised terms; (4) the concrete requirements were not set out in the 'normative document', but were instead implemented by a sub-office of the government in the form of an 'oral notice'; (5) it was not publicly accessible. 'Normative documents' of this kind are widely used at local levels.

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167 Randall Peerenboom, 'Ruling the Country in Accordance with Law-Reflection on the Rule and Role of Law in Contemporary China', *Cultural Dynamics*, 1999-3.

168 Since the 'normative document' in this case was never published or made publicly accessible through official channels when it was adopted, the source of this case comes from a special report published in the *Southern Weekend* newspaper. In September 2004, however, the auto importers brought their complaints to the courts in Hainan province. The judgments from the intermediate people's court of Haikou city and the high people's court of Hainan province provide some extra information on the fact of this case. 'Administrative Ruling of the High Court of Hainan Province', Case Number: [2005] Qiongxing Zhongzi No. 53, 23 May 2005.

#### *2.4.2.1 Questionable Legality of Normative Documents*

If order is to be predicated on laws, there must be a way of verifying whether they are valid and legally binding.[169] The criteria suggested by Peerenboom are useful for verifying the legality of normative documents: (i) they are made by an entity with authority to make laws; (ii) the entity was acting within its scope of authority; (iii) the entity followed proper procedures; and (iv) the regulations are not inconsistent with superior legislation.[170] Under this test, the legality of normative documents is questionable. First, normative documents are in many cases issued by entities without legal rulemaking rights. According to the Constitution and Legislative Law, the authorities with rulemaking rights include the NPC, the Standing Committee of the NPC, the State Council and its sub-ministries or departments, the local people's congress and government at a provincial level, or at the level of major cities (such as provincial capitals). However, normative documents are issued by administrative bodies at every level of the government, including those in small cities, counties and even towns. Second, since normative documents are not regarded as formal legislation, there are no standards or unified procedural rules to be followed for their adoption. The rulemaking procedures provided in national laws or regulations cannot be applied to them. Third, the requirement that 'the regulations shall not be inconsistent with superior legislation' is especially difficult to satisfy. Most normative documents are 'internal decisions' and not publicly accessible. As they are not transparent enough to be found, it is hard to judge whether they are conflicting. Even if they are found to contravene superior laws, the current review mechanism is not effective to correct them.[171] In practice, therefore, many normative documents contradict superior laws and regulations.

#### *2.4.2.2 Publication Requirements for Normative Documents*

As mentioned above, the Legislative Law publication requirements for all formal legislation do not apply to normative documents. Some local rules are progressively issued to regulate the adoption of such documents. The government of Guangzhou city, for instance, promulgated a local rule, the 'Guangzhou Administration Measures on Normative Documents', which entered into force on 1 April 2004.[172] This defines 'normative documents' as 'legal documents

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169 Randall Peerenboom, 'Ruling the Country in Contemporary China', 1999..

170 See Randall Peerenboom, 'Ruling the Country in Contemporary China', 1999.

171 There is an administrative mechanism for reviewing the legality of administrative rules. Conflicting legal documents issued by administrative organs can be corrected by administrative organs at a higher level. As explained in the discussion of market fragmentation problem, however, one of the reasons why this self-review mechanism is not effective is the common interests that are shared by these administrative organs. Although there is also a judicial review mechanism in China, it cannot be used to challenge administrative decisions with general binding force (i.e. administrative rules or regulations), but only to challenge administrative decisions for specific organizations, groups of people or individuals. This limitation is discussed in the following section.

172 'Guangzhou Administration Measures on Normative Documents' was issued on 15 December 2003 and entered into force on 1 April 2004. It was issued by the Guangzhou People's Government.

that can be used repeatedly and are issued by government and its sub-authority departments with a general binding force to the individuals, legal persons and other organizations'.[173] This definition gives 'normative documents' legal authority similar to laws. It provides some basic requirements for the adoption of normative documents. Normative documents may, for instance, take such forms as 'regulations', 'rulings', 'measures', 'opinions', 'decisions', 'notices' and so on,[174] and must not contradict the Constitution, laws, regulations, decrees and rules, or administrative decisions and rules from higher authorities.[175] Importantly, some transparency requirements have been added, whereby normative documents have to be published in the government policy journal, a newspaper circulated within the administrative jurisdiction and on the government's official website.[176] Normative documents also have to be enforced 30 days after publication.[177]

Similar provisions can be found in a rule recently issued by the government of Beijing city.[178] Some improvements have been achieved compared with the one issued in Guangzhou in 2004, especially in respect of transparency. This new rule emphasizes that normative documents must be published 30 days before enforcement, and those that have not been published cannot be sources of administrative activities.[179] Ordinary people have the right to access normative documents that have been published, and entities issuing normative documents have responsibilities to facilitate this by providing convenience in the form, for example, of free access to official versions of normative documents at the entities' locations.[180] The rule also states that the government's Documentation Bureau is the designated authority for providing free access to normative documents.[181]

The requirement for publication and free public access in the rule issued by the governments of Beijing and Guangzhou can be regarded as an important step forward in making the adoption of normative documents more transparent. However, the limitation is that this rule only regulates the adoption of normative documents in Beijing or Guangzhou. The transparency requirements in these regulations are not uniform, and those provided in Guangzhou are less stringent. Efforts to achieve transparency in the adoption of normative documents are still in a nascent stage, and unitary and consistent provisions are still lacking.

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173 Article 2 of 'Guangzhou Administration Measures on Normative Documents'.

174 Article 7 of 'Guangzhou Administration Measures on Normative Documents'.

175 Article 4 of 'Guangzhou Administration Measures on Normative Documents'.

176 Article 23 of 'Guangzhou Administration Measures on Normative Documents'.

177 Article 24 of 'Guangzhou Administration Measures on Normative Documents'.

178 'Beijing Administration and Supervision Measure on Normative Documents' was promulgated on 20 September 2005, and entered into force on 1 January 2006. It was issued by the Beijing People's Government.

179 Article 5 of 'Beijing Administration and Supervision Measure on Normative Documents'.

180 Article 6 of 'Beijing Administration and Supervision Measure on Normative Documents'.

181 Article 7 of 'Beijing Administration and Supervision Measure on Normative Documents'.

#### *2.4.2.3 Limited Supervision and Lack of Legal Remedy for Application of Normative Documents*

In China, administrative activities are divided into abstract administrative activities and specific administrative activities. While the former normally refer to the issuance of regulatory measures that may have binding force on the general public, the latter are administrative decisions affecting only a specific person or organization, such as an administrative punishment decision imposed on a certain enterprise. Having general binding force means normative documents are categorized as abstract administrative activities.

Under Chinese law, only specific administrative actions can be remedied by legal means, whereby individuals who are dissatisfied with specific administrative actions, irrespective of whether the administrative review mechanism has been exhausted, can file a court case against the specific administrative action. This means that judicial review in China is available only in respect of specific administrative activities. However, the adoption and enforcement of normative documents, as abstract activities, are not subject to any supervision by judicial organs.

Without the opportunity for legal remedies, all the supervision and remedies available in the case of normative documents have to be found within the administrative system. Both the Guangzhou and Beijing governmental rules discussed above, for example, allow any organization, enterprise or individual with an opinion on the validity and application of a normative document to send written application for a review to the 'supervisory body' – the higher administrative authority – for a final decision.[182] Take the transparency requirement as an example: if an administrative body enforces a normative document that has not been published, the administrative actions based on this normative document or the normative document itself may be revoked by a higher-level administrative body. However, internal administrative supervision has two shortcomings. Firstly, its direct and close relationship to the administrative body in question may hinder, in many cases, the higher administrative body to provide supervision and remedy with adequate fairness and efficiency. Secondly, many individuals and enterprises are reluctant, for fear of disrupting the internal relationship, to complain to the supervisory body. This makes it harder to identify and reveal problems in normative documents. This flaw in the Chinese administrative system means that the regulatory activities of administrative authorities (i.e. the adoption of normative documents) are poorly supervised, and transparency is therefore difficult to ensure.

182 Article 33 of 'Guangzhou Administration Measures on Normative Documents' and Article 18 of 'Beijing Administration and Supervision Measure on Normative Documents'.

## 2.5 OBSTACLES TO TRANSPARENCY ASSOCIATED WITH LEGAL CULTURE

The principle of transparency broadly derives from liberal principles of government accountability. Proceeding from tenets on human equality and natural law, the liberal tradition of political ideology asserts that government is essentially an agency of popular will.[183] A responsible agency is thus a typology by which regulators and their political superiors are accountable to the subjects of regulation, and as a result are expected to exercise regulatory authority broadly in accordance with norms of transparency and rule of law.[184] However, these regulatory norms are confronted by powerful forces of legal culture in the case of China. The norms that inform China's regulatory culture may be described in terms of 'patrimonial sovereignty'.[185] Governance is pursued by a sovereign political authority that remains largely immune to challenge.[186] Regulatory norms serve as instruments of the Party's policies of control, and the supremacy of the Party remains entrenched in the regulatory process even after twenty year of legal reform. 'Patrimonial sovereignty' is thus a typology by which regulators are accountable only to their bureaucratic and political superiors, and as a result have few obligations to heed the subjects of rule or the substance of regulation.[187] Under this ideology, political leaders and administrative agencies have responsibilities *for* society, but are not responsible *to* it.[188]

Keeping the above theoretical discussion of legal culture in mind, we have to establish the impact of the country's distinct legal and political culture on levels of transparency in China's legal and administrative system. Extensively adopted and poorly regulated 'normative documents' constitute a major obstacle to transparent rulemaking and a coherent legal system uniformly administered by the state. Analyzing the root cause of the existence of these normative documents may help shed some light on what the real challenges are for China in seeking to comply with WTO-required transparency.

As discussed above, normative documents are not recognized as formal legislation by the national laws and regulations, and they fall outside the rulemaking requirements. They may be issued by governmental organs that do not have the rulemaking power, and their application may not accord with legal requirements. The next question is where the legality of normative documents comes from or, in other words, what makes them valid and legally binding? The answer is not that they are issued in accordance with norms of the rule of law

183 Pitman B. Potter, 'Globalization and Economic Regulation in China: Selective Adaptation of Globalized Norms and Practices', *Washington University Global Studies Law Review* 2003-1.
184 Pitman B. Potter, 'Globalization and Economic Regulation in China', 2003.
185 Pitman B. Potter, 'Globalization and Economic Regulation in China', 2003.
186 Pitman B. Potter, 'Globalization and Economic Regulation in China', 2003.
187 Pitman B. Potter, 'Globalization and Economic Regulation in China', 2003.
188 Pitman B. Potter, 'Globalization and Economic Regulation in China', 2003.

and transparency requirements. A standard answer from ordinary Chinese people is that they are certainly 'legal' and that people have to obey them because they are issued by 'government'. It is not difficult to see that the legality of the normative documents comes from their issuing authorities themselves – the government or the Party. This once again demonstrates: (1) the supremacy of the Party's power, rather than the role of law, in the country; (2) that 'laws' or other legal documents are more like instruments implementing Party policy; the extensive adoption of informal 'normative documents' confirms the legal culture or tradition of the Party relying strongly on 'policy-like laws' in governance; in contrast to Western political ideology, where government is an agency of popular will, the situation in China could be described as one in which 'law' is an agency of the government or Party's will; (3) that the 'patrimonial sovereignty', or supremacy of the Party, weakens the norm of government accountability; in other words, governmental authorities are responsible only to their political superior and, as a result, the importance of transparency, which derives from government accountability, is also weakened.

Overall, the adoption of normative documents falling outside the formal legislation exaggerates the complexity and opacity of the Chinese legal system. Although their legality is questionable according to the provisions in the Constitution and relevant national laws governing the legislation, the extensive adoption of normative documents makes them *de facto* regulatory norms with general binding force at the local level. This may trigger many problems in this area, including unpublished internal decisions, conflicts between normative documents and with superior regulations and laws, and a strong 'policy' character that is subject to frequent change in line with changes in policy. All these problems create difficulties in seeking to improve transparency in China. Although some transparency requirements have been incorporated into administrative rules adopted by governments in several big cities, these rules have not yet been able to ensure the implementation of transparency requirements in a coherent and unitary manner. Therefore, the impediments to improving transparency in China's legislative regime are closely related to its institutional characteristics, including its administrative structure and legislative procedures, and to its distinct legal culture.

## 2.6 CONCLUSION

The difficulties in China's compliance with WTO transparency requirements are deeply embedded in its complex legislative structure and in the existence of under-regulated informal laws, as well as in the country's distinct legal culture. The sheer complexity of the legislative structure is a defining feature of the legal system's opaqueness. Legislative power has been delegated to multiple levels of agencies, and the legal status of legislative enactments adopted by local authorities is vague. Unresolved conflicts between legal enactments obstruct coherency and transparency in the Chinese legal system. The excessive existence of informal laws, such as normative documents issued by administrative agencies,

exacerbates the problem of non-transparency in the regulatory regime. The publication requirements provided for in formal Chinese laws simply do not apply to normative documents since they are not recognized as a formal source of law in China. In most cases, these documents are adopted arbitrarily by administrative authorities and are not publicly accessible. Moreover, the country's distinct legal culture also contributes to the difficulty of enhancing transparency in China's legal system. The heavy reliance of the Party and the government on policy-like laws for governance purposes, as verified by the extensive adoption of normative documents, demonstrates that the role of law has yet to gain supremacy of power in China. The norm of government accountability is weakened in this legal culture and, as a result, the importance of transparency, as a concept deriving from the norm of government accountability, is also weakened.

The transparency requirement provided for in Article X:1 was incorporated as a trading rule without objection, mainly because it imposed no extra obligations on the developed countries that drafted the GATT. For developing countries with substantially different legal and political systems, however, it imposes very intrusive obligations that require systemic redesign. As demonstrated by the institution-related difficulties faced by China, it is simply not realistic to expect China to be able to comply with the WTO-plus obligations in the Accession Protocol. Indeed the country is almost certain to breach them. Although a national journal has been established and officially made responsible for fulfilling the requirement in the Accession Protocol to publicize all trade-related rules, the scope of trade-related rules published in this journal, for example, is limited to rules issued at the central level. In the case of rules issued at local levels, China is currently not able to publish them in a single official journal due to the complexity and under-regulated status of these formal and informal rules. China's existing legislative and administrative system has been developed without regard for the principle of transparency. It will be hard to achieve the desired result simply by pushing China into undertaking commitments that are beyond the reach of its institutional capacity. Requiring a weaker member to undertake stricter commitments also seems irrational. Putting China's WTO-plus obligations aside, even enforcing the basic transparency requirement in Article X:1 is already difficult for the WTO. The DSB's enforcement of this Article to date does not suggest that the WTO is particularly keen to enforce this rule since the number of cases brought under this Article has so far been limited, and the DSB's interpretations have remained indeterminate. The institutional obstacles to China's compliance with the transparency requirement undoubtedly add some extra difficulties to the DSB's decision on whether to seek to enforce this Article strictly. What is clear, however, is that the DSB, as the case of China indicates, should apply this Article more cautiously in order to achieve a balance between national regulatory autonomy and the effectiveness of the trading system.

# Chapter 3

## Compliance with the Requirement of Uniform Administration of Application of Laws

## 3.1 INTRODUCTION

Following the requirement to publish provided in Article X:1, Article X:3(a) requires uniform administration of trade regulations. It stipulates that 'each member shall administer in a uniform, impartial and reasonable manner all of its laws, regulations, decisions and rulings of the kind described in Article X:1'.[189] The main function of this obligation is to ensure that WTO rules can have uniform effect within the territory of a member such that domestic trade regulations that incorporate WTO rules can be uniformly applied. The DSB's interpretation further clarifies that this rule requires members to ensure uniform administration of the application of trade laws within their territories; in other words, a trade rule must be applied consistently and predictably over time and in different places and circumstances.[190] The DSB has also interpreted paragraph 3 of the Article to mean that the outcome of a single case may not provide decisive evidence of a violation of this requirement.[191] The pattern of overall administration of the application of law is of particular concern under this requirement. This interpretation indicates that the requirement is a systemic rather than substantive obligation.

In addition to Article X:3 (a), China's Accession Protocol emphasizes the obligation to administer in a uniform way and requires the provisions of the WTO agreements and the Accession Protocol to apply to the entire territory of China. It specifies that rules of Chinese local governments shall conform to the obligations undertaken in the WTO agreements. It particularly refers to uniformity between the central government and local administration with regard to the application of trade rules. However, this chapter argues that the WTO uniform requirement imposed on China may not be helpful from the perspective of narrowing the gap between the central and local levels in terms of the application of laws, given that the WTO requires centralization and decentralization at the same time.

This chapter approaches the issue of 'uniform administration' in two steps.
Firstly, uniform administration requires more than an adjustment of the substantive contents of laws. It also requires fundamental changes in China with regard to the legislative and administrative institutions. Rather than studying the individual application of a trade rule that may or may not lead to violations of Article X:3(a), the first part of this chapter explains the pattern of China's overall regulatory framework. It discusses the fragmented institutional

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189 Similar obligations are also contained in some goods agreements, such as the Agreement on Rules of Origin, Articles 2(e) and 3(d), and the Agreement on Import Licensing Procedures, Article 1.3. Uniform administration of laws affecting trade in services is also subject to a similar obligation, insofar as the law relates to a sector where the member concerned has undertaken specific commitments, such as the General Agreement on Trade in Services (GATS), Article VI:1. Sharif Bhuiyan, 2007, p. 75.

190 *Argentina – Measures affecting the Export of Bovine Hides and the Import of Finished Leather*, Panel Report, 19 December 2000, WT/DS155/R, paras. 11.80 and 11.83.

191 Report of the Panel, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, 24 August 2001, para. 7.268.

framework and the central government's ability to promote uniform administration of the application of laws. The problem to be researched is, therefore, the extent to which central and local trade regulations in China are compatible with the requirement of uniform administration as stipulated in Article X:3(a).

Secondly, this chapter explains that the absence of a uniform administration affects substantive obligations under the WTO. A fragmented institutional framework may easily lead to diverging and conflicting trade rules within a single WTO member; this means that a single domestic market without trade borders is absent or highly deficient. Considerable trade distortion would be created if, for example, a sub-division of a WTO party (such as a province in China) introduced local import duties or imposed a technical barrier. Apart from the issue of whether such duties or barriers are WTO-compatible, the question arises as to how imported products and services can be offered national treatment, provided for in Article III GATT, if duties and barriers vary *within* a single WTO member.

Part I explains the uniform administration provision under the GATT and its interpretation, as well as China's commitments with regard to this obligation. It provides an overview of China's institutional framework as regards the uniform administration and examines the central government's efforts to eliminate non-uniform application of the central law that contests fragmenting measures. It also explains why these efforts are ineffective. Part II discusses the consequences of a deficient uniform administration: the problems and manifestations of market fragmentation. It examines how fragmentation prevents China from complying with WTO rules and in particular its inability to offer national treatment to imported goods and services.

## 3.2 REQUIREMENT OF UNIFORM ADMINISTRATION IN THE WTO AND OVERVIEW OF CHINA'S COMPLIANCE

### 3.2.1 Article X:3(a) and the Interpretations

Uniform administration of trade regulations as provided for in Article X:3(a), together with others provisions under Article X, has been described as the 'good governance' or 'proper administration' provision.[192] It differs from other WTO rules with direct trade liberalization effects in that it requires due process enhancement of members' governmental and regulatory systems. It is considered an important guarantee for the effectiveness of substantive WTO rules and fairness to individual traders and businesses.[193] However, this

192 Friedl Weiss, 2007; William Davey, 'GATT Article X: Transparency and Proper Administration', in William Davey (ed.) *Enforcing World Trade Rules: Essays on WTO Dispute Settlement and GATT Obligations*, Cameron May, 2006, pp. 209-316.

193 Sharif Bhuiyan, 2007, p. 84.

obligation has so far attracted relatively little attention.[194] To understand its meaning and scope, the way it has been interpreted in the AB and Panel rulings has to be examined.

During the GATT years, violations of Article X:3(a) were typically pleaded only as 'add-ons'[195] or subsidiary matters[196] to other more promising legal claims of violations of WTO rules. WTO and GATT panels have habitually refused to rule on Article X claims where a measure has already been found to violate another, more substantive GATT or WTO obligation.[197] In, for instance, *Japanese Measures on Imports of Leather*, the United States argued, as a subsidiary matter, that Japan had also nullified or impaired benefits under Articles X:1 and X:3 GATT.[198] Typically, however, in view of the finding that the disputed import quotas already violated Article XI GATT, the Panel found it unnecessary to make a finding on this matter.[199] The Panel's reluctance to address Article X can be partially attributed to the fact that the initial focus of the GATT was on reduction of tariffs and elimination of quotas and other border measures.[200] The Panel, and probably the GATT contracting parties, did not find proper administration of Article X to be of primary importance.[201]

The Panel's attitude seemed to change after the creation of the WTO. In the *Argentina – Hides and Leather* case, the panel clarified the interpretation of Article X:3(a).[202] In many disputes since then, both the AB and the Panel have demonstrated interest in interpreting this provision. Firstly, the AB adopted a *substance/administration* distinction to define the scope of uniform administration obligation. It ruled that Article X:3(a) targets a particular *manner of administration* of the application of national laws rather than the *substantive content* of those laws. In, for instance, the *EC – Banana* case, the complaints challenged the EC's banana import regime as a violation of Article X:3(a) because it imposed different

194 Robert Howse, 2003, p. 91.

195 Friedl Weiss, 2007.

196 Padideh Ala'I, 2007, p. 118.

197 Warren Maruyama, 2003.

198 Report of the Panel, Japanese Measures on Imports of Leather, paras. 26, 28, 30 & 57, L/5623-31S/94, 15-16 May, 1984, GATT 31 B.I.S.D. 94.

199 Report of the Panel, Japanese Measures on Imports of Leather, para. 57, L/5623-31S/94, 15-16 May, 1984. See generally Report of the Panel, *Republic of Korea – Restrictions on Imports of Beef – Complaint by the United States*, L/6505-36S/268, November 7, 1989, GATT B.I.S.D 36S/286; *Canada – Import Restrictions on Ice Cream and Yoghurt*, December 5, 1989, 36 B.I.S.D. pp. 68 & 92. See Friedl Weiss, assisted by Silke Steiner, 'Transparency as an Element of Good Governance in the Practice of the EU and the WTO: Overview and Comparison', *Fordham International Law Journal*, vol. 30, 2007.

200 Padideh Ala'I, 2007, p. 118.

201 Padideh Ala'I, 2007, p. 118.

202 Report of the Panel, *Argentina – Measures Affecting the Export of Bovine Hides and the Import of Finished Leather*, WT/DS155/R, 19 December 2000. It emphasized the concept of 'uniformity' relating to the requirement in Article X:3(a) GATT that laws and regulations shall be administered in a uniform, impartial and reasonable manner. Friedl Weiss, 2007.

import licensing regimes for bananas, depending on their origin.[203] In the Panel's view, this constituted a lack of uniform administration. The AB, however, reversed the Panel's finding of a violation. It stated that Article X:3(a) only required uniformity in the administration of laws and did not address the discriminatory content of a measure.[204] The AB's interpretation clarifies the scope of Article X:3 (a): it relates always to the application of laws, and not to the substantive content of laws.[205] In other words, the *consistency of laws* cannot be challenged, whereas the *consistency of the application of laws* can be challenged. Conflicts between Chinese law at a central level and a local rule will not, for instance, be regulated by this Article. If, however, the central law is applied differently in Beijing and Shanghai, this inconsistent application of law can be challenged under Article X:3(a).

Secondly, uniform administration must be distinguished from the non-discrimination requirement and cannot be seen as a broad anti-discrimination provision. As stated in the *EC – Banana* case, this provision does not address the discriminatory nature of a measure and therefore does not preclude the EC from imposing two different import licensing systems on similar products imported from different members. Article X:3(a) deals only with the outcome of the non-uniform administration, i.e. inconsistent application of laws. To the extent that measures are discriminatory, they should be examined under non-discrimination provisions, such as Most Favored Nation and national treatment clauses.[206] While discrimination may be applicable with regard to two or more different parties, non-uniform administration can happen to the same person at different times and in different places.[207] For example, it would be discrimination if Shanghai Customs treated exporter A differently from exporter B. However, if exporter A was treated differently by Beijing Customs than it was by Shanghai Customs, or was treated differently at different times by the same Customs, this could not be defined as discrimination since there is only one party. In this case, the different treatment imposed on exporter A could be the result of inconsistent application of Customs law.

The final issue relates to the establishment of violations of the uniform administration requirement. Will one case of the different application of law necessarily lead to a

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203 Report of Appellate Body, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, 25 September 1997.

204 Report of Appellate Body, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, 25 September 1997, para. 200.

205 Report of the Appellate Body, European Communities-Selected Customs Matters, WT/DS315/AB/R, 13 November 2006, paras. 190-217. In this case, the AB made one exception to the interpretation that substantive content of law cannot be challenged under Article X:3(a), i.e. if the law in question specifically regulates the administration of application of laws within a member, the substantive content of this law may be challenged under this Article. See report of the Appellate Body, *European Communities – Selected Customs Matters*, WT/DS315/AB/R, 13 November 2006, paras. 190-217.

206 Report of Appellate Body, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, 25 September 1997, para. 200.

207 Report of the Panel, *Argentina – Measures Affecting the Export of Bovine Hides and the Import of Finished Leather*, WT/DS155/R, 19 December 2000, paras. 11.81-11.84.

demonstration of non-uniform administration? The Panel appeared to be hesitant. In the *US – Hot-Rolled Steel Products* case,[208] Japan claimed a failure of uniform administration by US anti-dumping law since the US authorities made different decisions in this case compared to others.[209] The Panel stated that the US actions were taken in the context of a single anti-dumping investigation and it doubted whether the anti-dumping measure in this dispute could be considered a measure of 'general application'. Article X is only applicable to laws, regulations, judicial decisions and administrative rulings of 'general application'.[210] In this context, the Panel noted that Japan had not even alleged, much less established, a pattern of decision-making with respect to the specific matters raised that would suggest a lack of uniform, impartial and reasonable administration of the US anti-dumping law.[211] It ruled that:

> While it is not inconceivable that a Member's actions in a single instance might be evidence of lack of uniform, impartial, and reasonable administration of its laws, regulations, decisions and rulings, we consider that the actions in question would have to have a significant impact on the overall administration of the law, and not simply on the outcome in the single case in question.[212]

The Panel's ruling suggested that demonstrating one case of non-uniform application of domestic law may not be sufficient to establish a violation of Article X:3(a). Rather, a pattern of such behavior needs to be shown, not simply the outcome of a single case. The Panel explicated the 'pattern' requirement in the more recent *EC – Customs Matters* case,[213] stating that the non-uniform administration in question should result in an actual or possible future adverse impact on the trading environment.[214] Moreover, as the AB emphasized in the same case, complaints needed to establish causality between differences in the application of legal provisions and the country's non-uniform administration. Differences in the application of legal provisions may not necessarily be the result of non-uniform administration. They may stem from exercises of lawful discretion in the application of law by different regions

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208 Report of the Panel, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, 24 August 2001.

209 Japan argued that five separate actions or categories of action taken by the US authorities in the course of making their decision to impose the challenged final anti-dumping duty measure demonstrated a lack of uniform, impartial and reasonable administration of the US anti-dumping law. Report of the Panel, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, 24 August 2001, para. 7.267.

210 Report of the Panel, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, 24 August 2001, para. 7.266.

211 Report of the Panel, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, 24 August 2001, para. 7.268.

212 Report of the Panel, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, 24 August 2001, para. 7.268.

213 European Communities-Selected Customs Matters, WT/DS315/R, 16 June 2006.

214 European Communities-Selected Customs Matters, WT/DS315/R, 16 June 2006, para. 7.154.

or departments of one country. Therefore, showing inconsistent application of a legal provision within a WTO member may not be enough to establish a violation of the uniform administration commitment. Solid evidence proving that the inconsistencies are actually caused by the member's non-uniform administration is required. Moreover, in the above example of exporter A, the different treatment imposed on exporter A by different Customs within one country could be the outcome of inconsistent application of one specific Customs law. However, it could also be caused by substantively different local Customs rules, and Clearly, inconsistency of domestic laws is not the target of Article X: 3(a). The 'pattern' requirement and solid evidence for causality make challenging Article X:3(a) a difficult task. While it demonstrates the Panel and the AB's reluctance to apply Article X:3(a) strictly, their rulings in the above recent case make it increasingly clear that it is possible to challenge WTO-consistency of laws and application of laws under Article X:(a), while the question of whether an act amounts to non-uniform administration is decided against more specific standards.

### 3.2.2 China's Commitments in the Accession Protocol

The cautious approach adopted by the Panel and the AB for the application of Article X:3(a) stands in interesting contrast to the ambitious requirements of uniform administration provided for in China's Accession Protocol, as shown in the table below. The Accession Protocol provides a separate section entitled 'uniform administration', which has much greater breadth than Article X:3(a). While Article X:3(a) GATT only requires uniform administration of the application of laws in the field of trade in goods, the provision in China's Accession Protocol applies to all measures affecting trade in goods, services, TRIPS matters, and the control of foreign exchange. It also requires explicitly that all trade rules, not only those issued by the central government, but also those issued or applied by local governments at sub-national level, must be applied and administered in a uniform, impartial and reasonable manner. This commitment signifies the major concerns of the trading partners in China's accession negotiations about the consistency of application of laws at Chinese central and local levels. In order to ensure better conformity of local rules, China has also committed itself to establishing a mechanism for individuals and enterprises to bring cases of non-uniform applications of the trade regime to the attention of the national authorities.

**Table 4: China's Commitments on Uniform Administration--Comparison of Regular Requirement**

| Regular Uniform Administration Requirement – GATT Article X:3(a) | China's Uniform Administration Obligations committed to in the Accession Protocol |
|---|---|
| Uniform administration of application of laws related to trade in goods | Uniform administration of laws related to trade in goods, services, TRIPS, and control of foreign exchange[215] |
| | Conformity of local regulations, rules, and other measures with the WTO agreement and the Accession Protocol[216] |
| | Establishment of a mechanism under which individuals and enterprises can bring cases of non-uniform application of the trade regime to the attention of the national authorities[217] |

By targeting the lack of conformity in the application of laws in China, these commitments expand the coverage of Article X:3(a) and require China to make institutional improvements in its manner of administering the application of laws. These commitments are certainly ambitious, but whether they are a feasible and realistic means of bringing about real improvement depends on various indigenous conditions of China. One possibility would be for China to comply with the letter of these requirements, but with no substantial change in its problematic application of law in practice. The Chinese regulatory framework and the structure of its administration of the application of law are examined in detail in the following part of this chapter in order to offer valuable insight into the seriousness of the challenge China is facing in complying with these obligations and to establish whether these commitments are realistic and feasible.

215 Accession Protocol, 2(A)2.
216 Accession Protocol, 2(A)3.
217 Accession Protocol, 2(A)4.

## 3.2.3 Uniform Administration in China – General Obstacles in Institutional Arrangements and Regulatory Regime

### *3.2.3.1 Overview of Institutional and Regulatory Framework with regard to Uniform Administration*

#### *Decentralization and Central-Local Relationship*

Many of the difficulties in China's uniform administration stem from the diverse and fragmented nature of its entire society.[218] Traditionally, China has relied on its provinces to govern local populations. Within the provinces, territories are divided into over two thousand county-level divisions and forty thousand township-level divisions managed by local governments.[219] In many political systems, the hierarchical territorial power, which is designed for effective management of political control, economic development, social welfare and administrative efficiency, may pose serious problems for the national-level government if sub-national units are unwilling to comply with central directives.[220] While implementation slippage and local recalcitrance may be ubiquitous in many political systems, they are more likely to have a severe impact in developing countries and reforming socialist systems as these societies have few effective institutions and little experience in handling decentralized structures of interest coordination and policy execution.[221] The prevalence of local disparities in China, and the decentralization reform launched in the 1980s, has allowed an economic and administrative system of fragmentation to evolve.

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218 For a discussion of the fragmented nature of China's economic system, see Sandra Poncet, 'A Fragmented China: Measure and Determinants of Chinese Domestic Market Disintegration', *Review of International Economics*, 13(3), 2005. For a discussion of the fragmented nature of China's legal system, see Anthony R. Dicks, 'Compartmentalized Law and Judicial Restraint: An Inductive View of Some Jurisdictional Barriers to Reform', in Stanley B. Lubman (ed.) *China's Legal Reforms*, Oxford University Press, 1996. For a discussion of the fragmented nature of China's social and administrative system in general, see Zheng Yongnian, *De Facto Federalism in China – Reforms and Dynamics in Central-Local Relations*, World Scientific Publishing, 2007. Some literature, although not adopting the term of 'fragmentation', also refers to the decline of central control and difficulties in management of local issues through the discussion on 'localism', 'local autonomy' or 'local corporatism'. See, for instance, Pitman B. Potter, 'Foreign Investment Law in the People's Republic of China: Dilemmas of State Control', in Stanley B. Lubman (ed.), *China's Legal Reforms*, Oxford University Press, 1996.

219 www.gov.cn.

220 Jae Ho Chung, *Central Control and Local Discretion in China – Leadership and Implementation During Post-Mao Decollectivization*, Oxford University Press, 2000, p. 1.

221 This problem of 'governability' has been highlighted in association with such concepts as state capacity, regime legitimacy, and authority erosion. Scholarly attention is increasingly shifting toward local levels of government and their roles in the complex policy process. Similar concerns have also been voiced with regard to the state capacity and governability of China in recent years. Jae Ho Chung, 2000, p. 2.

By the late 1970s the inefficiency of centralized planning became increasingly clear. The Chinese central government consequently decided to reform by decentralizing its fiscal policies and implementing a revenue-sharing rearrangement between the various levels of authority in order to encourage local initiatives and economic growth.[222] This decentralization policy decreased the central government's share of revenue and encouraged local fiscal autonomy, while at the same time allowing local governments to retain significant amounts of surplus revenue, thereby creating an incentive to maximize local economic activities.[223] The decision to decentralize was based *inter alia* on the presumption that local governments were better positioned to effectively utilize information pertaining to their respective jurisdictions.

The decentralization endowed local governments with more and more discretion in economic policy-making and in many cases placed them outside the reach of the central government's coercion.[224] Even if the central government was able to exercise political control over the provincial leadership through the Party's *nomenklatura* system,[225] it does not have effective mechanisms to exercise control over local government officials below the provincial level.[226] In fact, some scholarly discussions have described the central-local relations in China as *de facto* federalism,[227] based on the observation that, in a behavioral sense, China's central-local relationship satisfies three conditions. Firstly, it has a hierarchical political system in which the activities of government are divided between the provinces and the center in such a way that each kind of government has some activities on which it makes

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222 Gregory H. Fuller, 'Economic Warlords: How De Facto Federalism Inhibits China's Compliance with International Trade Law and Jeopardizes Global Environmental Initiatives', *Tennessee Law Review*, Spring 2008.

223 Gregory H. Fuller, 2008.

224 Zheng Yongnian, 2007, p. 40.

225 The party achieves control of appointments of civil servants through the *nomenklatura* system. Under this system, there are two types of lists: lists with positions for which the party controls the appointment, and lists of candidates for such positions. The lists are drawn up by the party. The *nomenklatura* system operates for important positions that the party deems necessary to control. Burns was the first to describe the way in which the originally Soviet system of *nomenklatura* functioned in China. J. Burns, *The Chinese Communist Party Nomenklatuna System: A Documentary Study of Party Control of Leadership Selection*, Armonk, New York: M.E. Sharpe, 1989.

226 Zheng Yongnian, 2007, p. 246.

227 For a discussion of China's *de facto* federalism, see Montinola Gabriella, Qian Yingyi, Weingast Barry R., 'Federalism, Chinese Style: the Political Basis for Economic Success in China', *World Politics*, vol. 48, 1995; Dougherty Sean M., MacGuckin Robert H., 'Federalism and the Impetus for Reform in China', *China Law and Practice*, vol. 16, 2002; Zhu Suli, 'Federalism in contemporary China: A Reflection on the Allocation of Power between the Central and Local Governments', *Singapore Journal of International & Comparative Law*, vol. 7, 2003; Zheng Yongnian, 2007; Foley Thomas B., 'A Developing Revolution?: Disputing De Facto Federalism in China', *Hong Kong Law Journal*, vol. 37, 2007. In fact, the term 'federal China' is gaining popularity among Chinese dissident scholars, suggesting that China should adopt federalism to solve issues of national integration such as those relating to Taiwan, Hong Kong, Tibet and Xinjiang.

the final decisions.[228] Secondly, inter-governmental decentralization is institutionalized to such as degree that it is becoming increasingly difficult, if not impossible, for the national government to unilaterally impose its decisions on the provinces and alter the distribution of authority between governments.[229] Thirdly, the provinces have primary responsibility for the economy and, to some extent, politics within their jurisdiction.[230]

Although China has constitutionally remained a unitary state from a formal institutional perspective, power is, in a practical and behavioral sense, divided between the center and the provinces. Some powers, such as foreign policy, national defense and family planning belong exclusively to the central government, and it is very difficult for local governments to have a say on these matters.[231] Other matters, such as local public security, road construction and school building, are exclusively dictated by local governments.[232] Most economic matters are handled exclusively by local governments. For example, foreign direct investments and out-flowing investments below a certain limit are decided by local governments. Other powers are shared by the center and the provinces.[233] The research of Zheng Yongnian provides good annotations on the division of power between the center and the provinces, which is essentially governed by the three avenues of coercion, bargaining and reciprocity.[234] Coercion is defined as a process in which the center employs coercive means, such as the *nomenklatura* system and massive campaigns, to solicit compliance from the provinces. Coercion is unilateral, aiming at guaranteeing central control over the provinces and strengthening the unity of the nation. Bargaining is a process in which the two actors resolve conflicts between each other through various forms of bargaining. A key element in the bargain is that the provinces receive certain institutionalized or *ad hoc* benefits in return for guarantees by provincial officials that they will behave in certain ways on behalf of the center. Reciprocity can be defined as a process in which the two actors achieve voluntary cooperation between themselves through self-adjustment and deliberation. These methods are seen as constituting informal institutions that have created a decentralized *de facto* federal system of norms and rules in Chinese central-local relationship over the past three decades.[235]

It is worth noting that the exposition of the central-local power division is helpful in clarifying the debate on lack of capacity or lack of willingness in respect of China's difficulties in WTO compliance. Compliance with a specific WTO agreement may involve a set of issues related

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228 Zheng Yongnian, 2007, p. 39.

229 Zheng Yongnian, 2007, p. 40.

230 Zheng Yongnian, 2007, p. 40.

231 Zheng Yongnian, 2007, p. 40.

232 Zheng Yongnian, 2007, p. 40.

233 Zheng Yongnian, 2007, p. 40.

234 For a detailed discussion on how *de facto* federalism works in China through the three institutions of coercion, bargaining and reciprocity, see Zheng Yongnian, 2007, p. 53.

235 Zheng Yongnian, 2007.

to the complicated division of power between the center and the provinces, some of which are within the central government's coercive control and the rest of which are subject to bargaining with the local governments. If the non-compliance originates from the locally dictated zone, it is difficult to judge whether the central government is unable or unwilling to achieve the compliance. If the non-compliance originates from the centrally dictated zone, it is more likely that the non-compliance is due to a lack of willingness on the part of the central government. Therefore, any one-sided argument in the debate, which oversimplifies the facts, should be avoided.

### *Fragmented nature of the legal system per se*

The fragmented nature of the legal system *per se* also inhibits China's administration of the application of laws. This characteristic is determined mainly by legislative disorder (diverse administrative agencies and local authorities with overlapping powers in law-making), conflicts of law, inconsistency in the interpretation and implementation of law, and jurisdictional diversity (various units of local governments with jurisdictional power of their own).[236] Although the formal attributes of a unitary legal system have always been insisted upon in China, the practical problems include some of the worst disadvantages of federal legal systems, without the appropriate legal and political machinery even to resolve the resulting conflicts and tensions, far less to unify the law.[237] The lack of differentiation between the legislative, administrative and judicial functions of the various departments of the state leads to diversity in law-making and law implementation.[238] One of the consequences of this diversity of law-making and law-finding authority within the same legal system is excessive fragmentation, not merely of legislative, judicial and administrative jurisdiction, but ultimately of the law itself.[239]

During the fifteen years since the country began to open its doors to foreign investment, the geographical and departmental diversity of law-making and decision-making bodies has become an increasingly notorious "Chinese characteristic" of the legal system.[240] It leads to progressive fragmentation of the substantive law with the promulgation of each new and increasingly specialized enactment, as often as not including detailed implementing rules subject to the exclusive interpretation of the single department.[241] As well as inter-local and inter-departmental conflicts of law, local authorities also have substantial discretion to interpret regulations and are inclined to interpret and enforce regulations based on

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236 The fragmented nature of the Chinese legal system has been well documented. See, for example, Stanley B. Lubman, '*Bird in a Cage*', 1999; Anthony R. Dicks, 2008.

237 Anthony R. Dicks, 1996, p. 84.

238 Anthony R. Dicks, 1996, p. 84.

239 Anthony R. Dicks, 1996, p. 84.

240 Anthony R. Dicks, 1996, p. 84.

241 Anthony R. Dicks, 1996, p. 84.

parochial concerns rather than regulatory intent,[242] which exacerbates the inconsistency of law implementation. In a 1992 survey of American business executives with operations in China, 'lack of uniformity and consistency in interpreting and implementing rules and regulations' was a specifically cited problem.[243]

In short, the problems inherent in the Chinese legal system, i.e. conflicting law-making and inconsistent law implementation, compounded with the problem of the extent to which central government can influence local governments, constitute an institutional obstacle to the uniform administration of the application of law and in turn severely undermine the effectiveness of laws and regulations as an institutional mechanism for state regulation. While decentralization is institutionalizing local autonomy and fostering economic growth in China, it is also intensifying local rivalries in the process. The central government effectively traded a substantial degree of regulatory and policy-making power in exchange for rapid industrialization. The transfer of power empowers local leaders to shirk their critical enforcement duties in favor of enhancing their own political reputations through economic growth.[244] Importantly, the tension between local economic growth and national regulation has been exacerbated by China's membership of international agreements (such as the WTO agreements) and the related commitments. On the one hand, being compliant with international agreements requires further decentralization of many economic activities to local governments (foreign investment, for instance), thus making it increasingly difficult for the central government to access local economic resources. On the other hand, it also requires the center to be able to regulate local economic activities in order to comply with international agreements. In this regard, China's WTO membership affects its central-local relationship by creating two opposing forces that act as impediments to efforts uniformly to regulate compliance within the territory.

#### *3.2.3.2 Central Government's Unsuccessful Efforts to Enhance Uniform Administration*

The central government has undertaken formal measures to enable administration to be conducted in strict accordance with law, and has taken some major initiatives to deal indirectly with certain problems in the implementation of law. In order, for instance, to stop local governments' protective trade barriers that fragmented the national market, the central authority promulgated its first legislation outlawing the protective local measures and regulating *ultra vires* administrative actions at local levels in 1993. Under this legislation, 'governments and their subordinate departments shall not abuse their administrative powers to force others to buy the goods from the designated operators and to restrict the lawful business activities of other operators. Governments and their subordinate departments shall not abuse their administrative powers to restrict the inflow

242 Pitman B. Potter, 'Foreign Investment Law in China',1996.

243 'The Council's investment initiative', *China Business Review*, September-October, 1992, pp. 6-10.

244 Gregory H. Fuller, 2008.

of goods from other regions of the country into the local market or the outflow of local goods to markets of other regions of the country'.[245] However, this legislation has failed to put an end to local protective measures. Being more like a mere statement of the central authority's determination, this provision is possibly not being effectively enforced due to its ambiguous language and the lack of detailed implementing rules. Since the local protective measures continued to operate, the central government in 2001 issued a more specific law, the Provision on the Prohibition of Regional Blockades in Market and Economic Activities[246] (Provision of Regional Blockades). This states that, in order to establish a unified market, no authority or individual, in compliance with the requirements of state laws and regulations, shall obstruct the market access of goods from other localities.[247] Local governments at all levels shall ensure the elimination of market blockades and local protectionism.[248] Any regulation or provision issued by local governments that contradict this Provision shall be revoked or rectified.[249] The Provision also states that any other measures that are not necessarily regulatory actions of local governments, but *de fac*to restrict the normal flow of goods between different regions in China shall be prohibited and revoked.[250]

Although the Provision of Regional Blockades only prohibits regional blockades, for the purpose of maintaining a uniform national market for fair competition, it sends a clear signal to local authorities that local protectionism, one of the most serious problems facing uniform administration, is not in the national interest and nor will it continue to be tolerated by the central government.[251] However, the Provision of Regional Blockades has not been effectively enforced. Typical of the pragmatic solutions produced in China, the adoption of the Provision has been *ad hoc* and piecemeal, and has largely avoided the underlying problems in the political system.[252] As discussed below, the problems identified in the Provision itself, which may result from the *ad hoc* arrangements, contribute much to the difficulties of enforcement.

The first problem relates to the hierarchy of the Provision. According to the five-tier hierarchy in China's legal system, the Provision, issued by the State Council, constitutes an 'administrative regulation' and is thus lower than the Constitution and laws promulgated by the NPC. It has been suggested that the Provision should be provided in laws rather than in administrative regulations since a higher hierarchy would in principle lead to better

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245 Article 7, Law against Unfair Competition, promulgated by the National People's Congress, September 1993.

246 The Provision of Regional Blockades was issued by the State Council, effective on 21 April 2001.

247 Articles 1-3, Provision of Regional Blockades.

248 Articles 1-3, Provision of Regional Blockades.

249 Articles 6-8, Provision of Regional Blockades.

250 Article 10, Provision of Regional Blockades.

251 Jianfu Chen, 'Implementation of Law in China – An Introduction', in Jianfu Chen, Yuwen Li and Jan Michiel Otto (eds.), *Implementation of Law in People's Republic of China*, Kluwer Law International, 2002, p. 19.

252 Jianfu Chen, 'Implementation of Law in China', 2002, p. 19.

enforcement.[253] This is especially true in the case of the enforcement of law that is designed to regulate the behavior of local authorities. In discussions in Chinese literature, local protectionism in the circulation of commodities is defined as an 'administrative monopoly', which allows the government to abuse its administrative power to limit or eliminate competition.[254] While a monopoly generally refers to an economic monopoly conducted by private enterprises in developed market economy countries, an 'administrative monopoly' is more representative of monopolies in countries undergoing the transition from a planned economy to a market economy.[255] These transition countries have traditionally had absolute control of economic activities by administrative authorities and lack the experience, as well as the mechanism, to handle administrative *ultra vires* in the process of decentralization and market economy reform. In order to achieve better compliance, the anti-protectionism regulations should be provided systemically in a national law, for instance an anti-monopoly law, instead of being scattered across provisions issued by the State Council and the subordinated departments.[256]

The second problem is the improper imposition of supervisory bodies. The implementation of the Provision relies mainly on administrative supervision. Although activities of administrative authorities can generally be challenged through judicial review, judicial intervention in the behavior of local governments is very limited due to Chinese judicial organs' lack of independence. Similar to many administrative regulations that regulate administrative activities, the Provision assigns the 'competent higher administrative authority' to supervise the observance by the local governments. The 'competent higher administrative authority' refers to governmental or administrative agencies at higher administrative levels than those who adopt market blockade measures prohibited in the Provision. If a local government (for example, a city government) issues a rule that allows certain market blockade measures, the rule will be rectified or revoked by a government at

253 See, for example, Huang Xin and Zhou Yun, 'Administrative Monopoly and Legislation on Anti-monopoly', *Chinese Legal Science*, No. 3, 2001; Yang Wei and Wang Weinong, 'Administrative Monopoly and its Legislation', *Zhejiang Social Science*, No. 2, 2003.

254 See, for example, Xu Guangyao, 'Regulation on Administrative Monopoly under the Anti-monopoly Law', *Chinese Legal Science*, No. 6, 2004; Feng Liping, 'Administrative Monopoly and Anti-Monopoly Legislation in China', *Journal of Zhejiang University (Humanities and Social Science Edition)*, No. 5, 1999; Huang Xin and Zhou Yun, 2001.

255 According to Jiang Yanjun, the countries in transition, represented by Russia and Eastern European countries, may have an administrative monopoly inherited from the planned economy. In the transition process, these countries promulgate anti-monopoly laws to regulate administrative monopolies. In Article 63 of Hungary's Law against Unfair Competition of 1990, for instance, it is stated that if a decision of administrative authorities undermines fair competition, the competition supervisor may, as one party, request a legal remedy.' Jiang Yanjun, 'Comparative Study on Administrative Monopoly and Anti-Monopoly Legislation in China and Foreign Countries', *Journal of China University of Political Science and Law*, vol. 20, No. 3, 2002.

256 Huang Xin and Zhou Yun, 2001; Xu Guangyao, 2004.

a higher level (for example, the provincial government that has jurisdiction over that city).[257] The flaws in the administrative enforcement mechanism are obvious. The higher authorities may have common interests with lower authorities, especially in the case of market blockade measures that are designed to protect local interests. The above 1993 legislation (Law against Unfair Competition), which briefly refers to local government restrictions on the normal flow of goods, in fact states that the Administration of Industry and Commerce (AIC) at all levels is the competent authority and the supervisor on the application of this law.[258] However, the AIC does not have adequate legal authority and independence to fight against local protection measures. In practice, the AIC faces frequent constraints from local governments, even in the supervision of normal economic monopoly cases, notwithstanding the administrative monopoly measures adopted by the government.[259] In spite of there being a common interest, the imbalance of information between lower authorities and their supervisors is another difficulty for supervisors seeking to rectify illegal practices. The lower authorities have substantial information on the protection measures adopted by them. In the case of an investigation, the higher authorities are reliant on the lower ones to provide relevant information. The transparency problem discussed in Chapter III makes the supervision of administrative authorities even more difficult.

The final problem relates to the lack of legal remedy and negligible administrative liability. The Provision does not provide any legal remedy for violations. The only consequence is administrative punishment. However, the administrative liability is too negligible to be a deterrent against illegal restrictive measures. According to Article 21 of the Provision, local governments or authorities under the provincial level that violate this Provision will be given public and written criticism by provincial governments or authorities; if provincial governments or authorities violate this Provision, the public and written criticism will be given to them by the State Council, while administrative sanctions such as demotion will be imposed on persons who have direct responsibilities. Both 'public written criticism' and 'administrative sanctions' appear not to be punitive enough to effectively prevent illegal practices of local authorities. Moreover, there is no procedure for imposing penalties. For instance, the kinds of administrative sanctions to be imposed in different situations are not defined in the legal provisions. As a result, the competent authorities have an excessive degree of flexibility in adopting these administrative sanctions to suit their own needs.[260]

The failure of the specific law adopted by the central government to enhance the uniform administration demonstrates some of the institutional obstacles that the central government

257 Article 7 of the Provision of Regional Blockade.

258 Article 3, Law against Unfair Competition, promulgated by the National People's Congress, September 1993.

259 Huang Xin and Zhou Yun, 2001.

260 Xu Guangyao, 2004.

is facing, including the absence of independent and effective enforcing agencies and remedies.

## 3.3 CONSEQUENCE OF DEFICIENCY OF UNIFORM ADMINISTRATION AND ITS IMPACT ON COMPLIANCE WITH WTO SUBSTANTIVE OBLIGATIONS

The central government's failure to ensure uniform administration results in the persistence of a unique phenomenon in China. In other words, market fragmentation. This means that a single market without trade barriers at local levels is absent or highly deficient. Local authorities seeking to protect their own markets impose duties and barriers on goods from other localities. While the *formulation* of the fragmented market can be attributed to various problems existing in China's economic and administrative system, the *continuance* of the fragmented market is largely the result of ineffective enforcement of the Provision on Regional Blockades issued by the central government. The existence of market fragmentation will affect China's compliance with the substantive WTO obligations, such as Article III GATT on national treatment.

### 3.3.1 Consequence of Deficiency of Uniform Administration – Market Fragmentation

To many people, China is an integrated economy. In other words, a centrally controlled economy with a single central government and a single currency in circulation. Economic integration, however, should be clearly distinguished from 'centralization'.[261] Centralization usually 'pertains to the allocation of decision-making authority or of command over information, not to the pattern of economic activity itself. In general, there is no necessary relationship between centralization and integration; a market economy is highly decentralized, but this decentralization does not imply that a market economy is not integrated'.[262] In other words, a centralized economy does not necessary imply that the economy is integrated.[263]

The key element to decide whether there is an integrated or single market is the factor mobility, i.e. free movement of goods, services, capital and personnel. The format of economic integration at an international level is an illustrative example of what constitutes

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261 Weixin Huang, *Economic Integration as A Development Device-The Case of EC and China*, Verlag Breitenbach Publisher, 1992, p. 47.

262 Lyons Thomas, *Economic Integration and Planning in Maoist China*, Columbia University Press New York, 1987; Weixin Huang, 1992, p. 47.

263 Weixin Huang, 1992, p. 47.

a single market. There are seen as being four theoretical types of international economic integration: free trade areas, customs unions, single/common market, and economic union. A *free trade area* is an agreement among member nations to remove all tariff and quantitative restrictions on mutual trade, but to retain their freedom with regard to determining their own policies vis-à-vis the outside world or non-participants.[264] GATT defines free trade areas as a group of two or more Customs territories in which the duties and other restrictive regulations of commerce are eliminated on substantially all the trade in products.[265] A *customs union* not only ensures free trade of products within a group of customs territories, but also applies to common external commercial regulations and duties on trade with territories not in the union.[266] A *single market* is a customs union which also allows for free mobility across member nations.[267] The Treaty establishing the European Economy Community formally recognizes this single market idea by spelling out the 'four freedoms': free movements of goods, persons, services and capital.[268] An *economic union*, which refers to the highest level of economic integration, is a single market that seeks complete unification of fiscal and monetary policies, i.e. participants must introduce a central authority to exercise control over these matters so that member states effectively become regions of the same nation.[269] El-Agraa provides a schematic outline of various forms of economic integration, including 'political union'. This gives a complete picture for the purposes of comparing their different functions.[270] For the purpose of discussion in this chapter, China, being considered a political union, has also been added to the following table to show its unusual character compared with that of normal economies.

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264 Miroslav N. Jovanović, *International Economic Integration*, Routledge, 1982, p. 9.

265 GATT Article XXIV 8 (b).

266 GATT Article XXIV 8 (a).

267 Ali M. El-Agraa, *Economic Integration Worldwide*, Macmillan Press, 1997, p. 2.

268 Jacques Pelkmans, *Market Integration in the European Community*, Martinus Nijhoff Publishers, p. 154. While the concept of a single market and a common market can be used interchangeably, a single market is sometimes differentiated as a more advanced form of common market since it envisions more efforts geared towards removing the physical borders, technical standards and fiscal barriers between the Members States of European Union.

269 Ali M. El-Agraa, *The European Union: Economics and Policies*, seventh edition, Prentice Hall, 28 January, 2004, p. 2.

270 Ali M. El-Agraa, 2004.

**Table 5: Various Forms of Economic Integration**[271]

| Scheme | Free intra-scheme trade | Common external commercial policy | Free factors mobility | Common monetary and fiscal policy | One government |
|---|---|---|---|---|---|
| **Free trade area** | Yes | No | No | No | No |
| **Custom union** | Yes | Yes | No | No | No |
| **Single/Common market** | Yes | Yes | Yes | No | No |
| **Economic union** | Yes | Yes | Yes | Yes | No |
| **Political union** | Yes | Yes | Yes | Yes | Yes |
| **…** | … | … | … | … | … |
| **China as a political union** | No | Yes | No | Yes | Yes |

The above table demonstrates that China's economic integration acts oddly compared to what is expected of a political union. In practice, although China has common external policy under the control of a single government, it does not have an integrated internal market. Neither free trade in goods nor mobility of production factors have effectively been achieved in the domestic market. The impediments to internal trade demonstrate that China is not economically integrated,[272] and this puts China outside any of the economic integration formats in the above table.

Many economic studies prove that there is a general lack of integration between regional markets in China. According to the findings of Poncet, Chinese consumers in 1997 bought 27 times more goods produced in their own province than goods from other provinces.[273] Using common assumptions about consumer behavior, she then computed the level of tariff that would be needed to produce this pattern if markets were perfectly integrated. Poncet

271 Ali M. El-Agraa, 2004, p. 1. Important Note: 'Free intra-scheme trade' in this table refers mainly to the free internal trade in goods and services. 'Free factors mobility' refers to the free movement of factors such as capital, labor, enterprises, technology, etc. The 'Four freedom' principle adopted by the EU contains both free trade in goods or services, and free factors mobility. It summaries those freedoms simply as four kinds of free movement: goods, services, persons and capital.

272 Weixin Huang, 1992, p.1.

273 Sandra Poncet, 'Measuring Chinese Domestic and International Integration', *China Economic Review*, 14, 2003. Sandra Poncet has conducted a great deal of research on Chinese domestic market fragmentation using a technique called 'border effects' to estimate the extent to which provincial borders deter trade inside China. Her works include 'A Fragmented China: Measure and Determinants of Chinese Domestic Market Disintegration', *Review of International Economics*, 13(3), pp. 409-430, 2005; Sandra Poncet, 'Domestic Market Fragmentation and Economic Growth in China', The 43rd European Congress of the Regional Science Association, Jyvsky, Finland, 27-30 August 2003.

found that goods crossing provincial borders in China faced the equivalent of a 51% tariff in 1997.[274] Barriers to trade *between* Chinese provinces turned out to be closer in magnitude to those on international trade than those on trade flows within a single country.[275] While Chinese reforms succeeded in promoting freer international trade, they failed in reducing the impediments to interprovincial trade.[276] This demonstrates the reforms' failure to promote domestic integration and the growing division of the Chinese domestic market into cellular submarkets.[277] Young made a striking conclusion in 2000 that 'over the past 20 years of economic reform, China has evolved into a fragmented internal market with fiefdoms controlled by local officials'.[278] While Zheng Yusheng concluded, based on the potential loss in output in Chinese provinces during 1978-2000, that market fragmentation was getting worse since the market economy reform,[279] Naughton found that the integration level between regions was actually increasing.[280] Bai Chongen was of view that although the integration level decreased in the earlier stage of the reform, it has increased dramatically in recent years.[281] In spite of different opinions on the extent of fragmentation, the existence of the problem is recognized by Chinese and foreign academics alike.

#### *3.3.1.1 Historical Background*

The current market fragmentation is partly a legacy of the cellular nature of the economy formulated under the planned economy of the 1950s to 1970s.[282] Before its open door policy in 1979, China was a centrally planned economy, in which most products were allocated and transferred by the central government throughout the entire territory in line with an economic plan. Because of a shortage of basic materials, a rationing system was established for allocating materials in each province.[283] Residents in every province were granted regional coupons for food, oil, clothes and so on. However, these regional coupons were

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274 Sandra Poncet, 2003.

275 Sandra Poncet, 2003.

276 Sandra Poncet, 2003.

277 Sandra Poncet, 2003.

278 Alwyn Young, 'The Razor's Edge: Distortions and Incremental Reform in the People's Republic of China', *Quarterly Journal of Economics*, November 2000.

279 Zheng Yusheng and Li Chonggao, 'Efficiency Loss Caused by Regional Fragmentation', *Chinese Social Science*, issue 1, 2004.

280 Barry Naughton, ;How much can regional integration do to unify China's markets?', in Nicholas Hope, Dennis Yang and Mu Yang Li (eds.), *How far across the river? Chinese Policy Reform at the Millennium*, Stanford University Press, 2003, pp. 204-232.

281 Bai Chongen, Du Yingjuan, Tao Zhigang, Tong Sarah Y, 'Local Protectionism and Industrial Concentration in China: Overall Trend and Important Factors', *Economic Research Journal*, issue 4, 2004.

282 Jiao Junpu, 'Relationship between Chinese Domestic Market Integration and Foreign Trade Benefits', *Journal of Lanzhou Commercial College*, vol. 20, No. 4, 2004; Yin Wenquan and Cai Wanru, 'The Genesis of Regional Fragmentation in China's Local Market and Countermeasures', *Economic Research Journal*, issue 6, 2001.

283 Yin Wenquan and Cai Wanru, 2001.

not able to circulate in other provinces. As a result, the thirty provincial-level divisions[284] were *de facto* thirty comparatively independent markets as products could not move freely in response to market demand, and any surpluses or shortages could be adjusted only in the central government's plan.[285] Thus, each administrative division had a separate vertical and direct relationship with the central government, with little horizontal liaisons between the individual divisions.[286] This cellular nature was a unique feature of the Chinese economy during that period,[287] and naturally led to a fragmented domestic market.

The market economy reform that started in the late 1970s was aimed at encouraging market forces as a guiding principle for product allocation, prices and movement, and at unifying previously isolated local markets into a single integrated market. However, the market fragmentation continued at different periods of the reform and for different reasons. In the early stages of the reform, China started running short of materials and products because of the low level of production capacity.[288] Local governments were reluctant to open their markets to other provinces, mainly because that they were afraid of the *outflow* of limited resources and products to other regions.[289]

The development of private and collective sectors under the economic reforms in 1980s resulted in a dramatic change in this situation; materials were no longer in short supply, and supplies of products started to exceed demand.[290] Thus, local market blockades shifted from contests for limited supplies of materials and resources to a struggle for market share.[291] Local authorities began to adopt measures restricting the *inflow* of products from other regions in order to ensure locally produced products retained their market share.[292] Many provinces drew up lists of goods which were banned from being imported and set up 'inspection posts' to collect taxes and fines.[293] The restrictions mainly affected

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284 Currently, China has 31 administrative divisions at provincial levels: 22 provinces, 5 special administrative autonomous regions (Guangxi, Ningxia, Inner Mongolia, Tibet and Xinjiang), and 4 direct-controlled municipalities (Beijing, Shanghai, Tianjin and Chongqin). During the 1970s, however, there were only 30 provincial-level administrative divisions as there were only 3 directly controlled municipalities.

285 Zhong Changbiao, *Studies of the impact of market fragmentation in transitional China on its international competition ability*, Shanghai People's Publishing House, 2005, p. 48.

286 Weixin Huang, 1992, p. 50.

287 Audrey Donnithorne, 'China's Cellular Economy: Some Economic Trends since Cultural Revolution', *The China's Quarterly*, No. 52, 1972.

288 Zhong Changbiao, 2005, p. 45.

289 Zhong Changbiao, 2005, p. 45.

290 Zhong Changbiao, 2005, p. 46.

291 Zhong Changbiao, 2005, p. 46.

292 Zhong Changbiao, 2005, p. 47; Zhao Yaping and Xiao Xiang, 'The Development of Theoretical Studies on China's Integrated Market', *Macroeconomics Studies*, issue 1, 2001.

293 Sandra Poncet, 'The Fragmentation of the Chinese Domestic Market – Peking struggles to put an end to regional protectionism', translated from French original by Peter Brown, *China Perspectives*, No. 55, September 2004.

manufactured goods, particularly television sets, household appliances, bicycles, stereos and other electrical equipment.[294] Local governments used all sorts of measures to implement their protectionist policies, including road blocks, the seizing of merchandise, *ad hoc* taxes, administrative charges, biased technical standards and bureaucratic red tape.[295] Outside firms faced enormous difficulties in purchasing premises, equipment and land, and in obtaining finance.[296] Nowadays, such local protective trade barriers aimed at restricting access of or competition from non-local products are the main manifestations of China's market fragmentation.

#### *3.3.1.2 Major Causes of Market Fragmentation*

The administrative and financial decentralization in the market economy reform in the late 1970s are seen as the main causes of market-fragmenting measures.[297] Firstly, the decentralization reform conducted in the early 1980s decentralized three kinds of powers to local governments: fiscal and taxation powers, investment and commercial project review powers, and administrative powers for state-owned enterprises.[298] In the case of the reform of the fiscal and taxation system, local governments now enjoy full autonomy over their fiscal revenues after they have paid the required amount to the central government.[299] Investment project review powers were also decentralized to local governments, which now enjoy broader rights to approve local investment projects.[300] In addition, the central government's administrative powers in respect of state-owned enterprises were transferred to local governments.[301]

Secondly, placing the emphasis on a self-reliant local economy motivates the local government to adopt local protection measures.[302] More economic autonomy means less

294 Sandra Poncet, 'The Fragmentation of the Chinese Domestic Market', 2004.

295 Sandra Poncet, 'The Fragmentation of the Chinese Domestic Market', 2004.

296 Sandra Poncet, 'The Fragmentation of the Chinese Domestic Market', 2004.

297 See, for example, Shi Lei and Ma Shiguo, 'The Formation Mechanism of Market Segmentation and Institutional Arrangements to Unify China's Market', *Journal of Renmin University of China*, No. 3, 2006; Yin Wenquan and Cai Wanru, 2001; Feng Xingyuan and Liu Huisun, 'Local Market Disintegration and Local Protectionism in China: Problems and Policy Recommendation', *Journal of National School of Administration*, No. 4, 2002; Liu Xiaoyong and Li Zhen, 'Empirical Study on Fiscal Decentralization and Regional Segmentation', *Journal of Finance and Economics*, vol. 34, No. 2, 2008.

298 Ma Xiuying and Zhao Ruyi, 'Studies on Causes of China's Local Market Fragmentation', *Contemporary Economic Research*, No. 4, 2008; Zhong Changbiao, 2005, p. 45; 'Countermeasures to Local Market Fragmentation', by research group under the Academy of Macroeconomic Research of State Development and Plan Committee, *Economic Research Reference*, issue 27, 2001.

299 Yin Wenquan and Cai Wanru, 2001.

300 Zhong Changbiao, 2005, p. 75.

301 Tang Yong, 'Integrated Market Institution and Regional Market Integration', *Finance and Trade Research,* No. 6, 2005.

302 Shen Liren and Dai Yuancheng, 'China's "Vassal Economy": Its Formation, Defects and Root Causes', Economic Research Journal, N0. 3, 1990; Feng Xingyuan and Liu Huisun, 2002.

economic dependence on the central government. Local governments need to develop economic self-reliance.[303] The pursuit of economic development by seeking to maximize fiscal revenues becomes a priority for local governments at every level.[304] Therefore, local enterprises' profits are among the top concerns of local governments, and accordingly the interests of local enterprises and governments are closely linked.[305] The local government's extensive administrative power in economic activities and the strong interest it has in protecting local profit-making creates conditions conducive to local interest-driven and institution-guaranteed protectionism. Under the dual strategy of seeking to minimize socio-economic instability and maximize tax revenues, local governments do everything possible to protect the enterprises within their locality.[306]

#### *3.3.1.3 Examples of Fragmenting Measures and Regional Trade Barriers*

Market fragmenting measures may have the same effect as tariff or non-tariff barriers. According to the 'Investigation Report on Domestic Local Protectionism' issued by the State Council, there are four major categories of restrictive measures relating to the movement of goods: quantitative restrictions; non-tariff barriers such as administrative inspections or technical standards; price controls and discriminative charges, and other informal and imperceptible restrictions.[307] The other four major categories of restrictive measures relate to labor and capital markets: raw materials restrictions on enterprises from other regions; restrictions on labor movements; restrictions on investment measures, and technique controls.[308] The level of their impact and their ranking in frequency of adoption are shown in the table below.

303 Ma Xiuying and Zhao Ruyi, 2008.

304 Wu Xun and Wang Li, 'Regional Market Segmentation during the Transition China: The Policy based on Game Analysis', *Journal of Yunnan University of Finance and Economics*, vol. 20, No. 5, 2004.

305 Ma Xiuying and Zhao Ruyi, 2008.

306 Feng Xingyuan and Liu Huisun, 2002.

307 'Investigation Report on Domestic Local Protectionism', by research group under the project of 'Chinese Single Market Establishment', Development and Research Center of the State Council, published in *Economic Research Reference*, issue No. 6, 2004; Chen Dongqi, Yin Wenquan and Zang Yueru, *Eliminating the Local Market Fragmentation*, Chinese Planning Press, November 2002, pp. 4-5.

308 'Investigation Report on Domestic Local Protectionism', by research group under the project of 'Chinese Single Market Establishment', Development and Research Center of the State Council, published in *Economic Research Reference*, issue No. 6, 2004; Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, pp. 7-8.

**Table 6: Forms and Impact of Local Trade Barriers[309]**

| Forms of local trade protection measures | Impact points | Ranking of frequency of adoption |
|---|---|---|
| Restrictions on labor movements | 57.7 | 1 |
| Other informal and imperceptible restrictions on market access | 55.7 | 2 |
| Technical barriers | 51.0 | 3 |
| Technique controls | 49.7 | 4 |
| Price control and discriminative charges | 47.3 | 5 |
| Quantitative restrictions on sale volumes | 46.0 | 6 |
| Restrictions on input of raw materials | 44.3 | 7 |
| Restrictions on investment measures | 42.0 | 8 |

The table shows that 'informal and imperceptible restrictions on market access', 'technical barriers', 'discriminative charges' and 'quantitative restrictions' are the most commonly applied restrictive measures in the movement of goods. Article 4 of the Provision on Regional Blockades also lists eight forms of market fragmentation measures that are prohibited under this regulation. These are:

- forced purchase or usage of products from local enterprises;
- setting a physical frontier or checkpoints on the administrative borders in order to restrict the market access of products from other regions;
- discriminatory charges or fees imposed on products from other regions;
- technical barriers – discriminatory technical standards or requirements and repeated inspection procedures;
- discriminatory licensing requirements imposed on products from other regions;
- discriminatory qualification requirements, review standards, or refusal to disclose necessary information to enterprises from other regions in order to restrict them from participating in local investment or other commercial bids;
- restrictions on investment activities of enterprises from other regions or preventing them from establishing a branch organization within the locality;
- other market fragmentation measures.

309 'Investigation Report on Domestic Local Protectionism', by research group under the 'Chinese Single Market Establishment' project, Development and Research Center of the State Council, *Economic Research Reference*, issue No. 6, 2004.

*Quantitative restrictions*

Quantitative restrictions are adopted by local authorities to prohibit market access of products from foreign provinces or, if not completely prohibited, to adopt quantitative restrictions in the local market.[310] Quantitative restrictive measures were extensively adopted during the mid-1990s, especially in markets, such as tobacco, that could be monopolized by local governments.[311] According to an investigation in a report entitled 'Countermeasures to local market fragmentation' prepared by the central government in 2001, the Henan and Anhui provinces completely prohibited market access of tobacco from Guizhou province since Guizhou province produces large volumes of tobacco and its tobacco products have a competitive advantage.[312] At the same time, some other provinces stipulated that the volumes of tobacco from Guizhou province sold in their local markets should not exceed 75% of the volume sold in a specific previous year.[313] In other cases, local authorities instructed local Industry and Commercial Administration employees to conduct *ad hoc* inspections of wholesale dealers and retailers to check whether they were selling prohibited products and, if so, authorized them to impose fines.[314]

*Discriminative charges*

Discriminative charges on non-local products represent another common example of local trade barriers.[315] They are frequently adopted in the automobile market.[316] Discriminative charges relating to market access, sales and usage have been imposed on automobiles produced in other regions.[317] Such charges are normally imposed on the basis of 'internal red-titled documents' or with the acquiescence of the relevant local authorities, without any formal documents attached.[318] Hubei province, for instance, issued a document in 1997, requiring all governmental organizations and enterprises under these governments to buy locally produced automobiles.[319] If they failed to do so, they would be denied license plates.[320] Between 1986 and 2000, an eastern coastal city adopted an 'auction with minimum prices' for individual buyers wishing to obtain license plates for new automobiles. The minimum

310 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 4.

311 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 4.

312 'Countermeasures to Local Market Fragmentation', by research group under the Academy of Macroeconomic Research of State Development and Plan Committee, *Economic Research Reference*, issue No. 27, 2001. A similar example is Jiangxi province, which largely prohibited market access of *Da Hongying* and *Liqun* tobacco from Zhejiang province. Zhong Changbiao, 2005, p. 50.

313 'Countermeasures to Local Market Fragmentation', 2001.

314 'Countermeasures to Local Market Fragmentation', 2001.

315 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 5.

316 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 5; Zhong Changbiao, 2005, p. 49.

317 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 5.

318 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 5.

319 'Countermeasures to Local Market Fragmentation', 2001.

320 'Countermeasures to Local Market Fragmentation', 2001.

price for locally produced automobiles was 20,000 yuan, compared with 90,000 yuan set for automobiles produced in other regions.[321] There are numerous other kinds of discriminative charges designed for the protection of local automobile industries.[322] Although their levels varies in the different provinces and regions, all these discriminative charges increase the costs of 'foreign' automobiles or other products, thus making them less competitive than local ones, and accordingly restrict or control market access to a certain extent.

### *Technical barriers*

Under the Agreement on Technical Barriers to Trade, technical barriers are various technical regulations, product standards and conformity procedures that are applied arbitrarily and used as an excuse for protectionism, and thus constitute barriers to trade. In international trade practices, technical barriers, including non-tariff barriers, have increasingly been used as one of the most influential protective trade measures. In Chinese domestic trade, technical barriers are also commonly adopted by local authorities. Local governments apply more rigorous technical standards or inspection procedures to non-local products that may compete with similar local products.[323] In some cases, local authorities may abuse their administrative powers to restrict market access by imposing discriminative technical requirements.[324] In other cases, they may organize high-frequency and lengthy provisional inspections of non-local products under the guise of quality supervision. These serve to restrict the market access of such products and delay their selling time until they are past their best. The inspections of a certain brand of mineral water, for example, delayed their entry into market until the expiration date.[325] These inspections were normally organized on an *ad hoc* basis and were required by some 'internal documents' or 'provisional decisions'.[326] They were disguised protective measures that made 'foreign' products subject to more onerous obligations than those applying to similar local products.

### *Other informal and imperceptible measures*

Market fragmentation may also take the form of informal or imperceptible protection measures, including *ad hoc* inspection and various measures provided in the 'internal red-titled documents'. As Table Two shows, these kinds of measures are adopted more often than others. The reason for this is obvious. The central government outlawed local trade protection measures years ago and so, instead of taking formal action, local governments

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321 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 128.

322 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, pp. 5-6.

323 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 4.

324 For a detailed case study, see Kong Xiangjun and Zhang Buhong (eds.), *Anti-unfair Competition Law and its Application through Case Analysis*, People's Court Publishing House, 1998, p. 114; Zheng Pengcheng, *Legal Control on Administrative Monopoly*, Peking University Publishing House, 2002, p. 51.

325 'Countermeasures to Local Market Fragmentation', 2001.

326 'Countermeasures to Local Market Fragmentation', 2001.

prefer to adopt temporary and imperceptible administrative acts in order to evade the administration of and punishment by the central government. Administrative inspections of non-local products may, for example, be conducted by *ad hoc* groups of officials, based on internal documents or memos, and sometimes on nothing related to a legal basis.[327] Beneficial treatment may also be offered to encourage the purchase of local products.[328]

### 3.3.2 Impact on Compliance with WTO Obligations

While the restricted internal trade may not impede China's participation in international trade[329], it will hinder China's compliance with the WTO rules. Localism (increased local autonomy and decline of central control), as demonstrated by the problem of market fragmentation, presents serious institutional difficulties to the central government in its efforts to ensure compliance with uniform administration of application of laws as required in GATT Article X:3(a). The continuance of the market fragmentation, after the central government's regulatory efforts to contest it, is largely the result of the latter's failure to conduct uniform administration of the application of the central law that aims to eliminate protective local trade barriers. This failure also shows evidence of local regulatory intervention and inaction, and that the central government has been unable to effectively administer and correct these local behaviors. Thus, the problems created by market fragmentation are typical examples to demonstrate a 'pattern' of non-uniform administration on application of laws, which is required to establish a violation to Article X: 3(a) by the WTO dispute settlement bodies.

The problem of market fragmentation may also obstruct compliance with several substantive WTO obligations. Generally speaking, the local protective measures are in conflict with the fundamental principles of trade liberalization and fair competition promoted by the WTO. Specifically, some substantive WTO rules can be effective only if free market access and movement of goods are allowed between different regions within the Chinese domestic markets.[330] The internal trade barriers also create unexpected trade barriers to foreign trading partners, especially as regards the internal distribution of foreign goods after they have been imported into China. US trade representatives have expressed concerns on this issue, claiming that:

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327 Chen Dongqi, Yin Wenquan and Zang Yueru, 2002, p. 5.

328 'Investigation Report on China's Domestic Local Protection – Preliminary Analysis of Sampling Survey on Non-Enterprises', by Research Group of 'Establishment of Chinese Single Market' under the Development and Research Center of the State Council, published in *Xinhua Digest*, issue 19, 2004.

329 Poncet's findings showed that, between 1987 and 1997, a decrease in inter-provincial trade flows went hand in hand with a rapid increase in Chinese provinces' involvement in international trade. Sandra Poncet, 'A Fragmented China', 2005, pp. 409-430.

330 Sandra Poncet, 'A Fragmented China', 2005, pp. 409-430.

> One of the priority issues that needs to be addressed in China's trading system is the elimination of trade barriers created by provincial and local governments.[331] Industrial policies that appear to limit market access of non-Chinese products and the promulgation of standards and other technical regulations that appear to favor locally produced products are among the key areas that continue to cause trade friction.[332]

The market fragmentation will particularly prevent China's compliance with the national treatment requirement provided in Article III GATT. As a fundamental non-discrimination principle pursued by the WTO, this stipulates that the treatment accorded to imported products shall not be less favorable than that accorded to similar domestic products as regards all internal taxes or charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products. Under China's market fragmentation, however, non-local domestic products may be discriminated compared to local domestic products. If there is no uniform treatment of domestic products within China's domestic market, there will be no "national treatment", and thus it will be extremely difficult, if not impossible, to judge whether imported products have received national treatment.

Although local trade barriers are not specifically imposed on imported products, they *de facto* result in less favorable treatment of imported products and impede their internal sale and distribution within China. The Report of the Working Party on the Accession of China has already stated that:

> Certain provisions of Chinese laws, regulations, administrative notices and other requirements could, directly or indirectly, result in less favorable treatment of imported products and thus be in contravention of the national treatment requirement under GATT. Even when such requirements only existed in relation to domestically produced goods, any de facto or de jure less favorable treatment of imported goods had to be eliminated in order to ensure full conformity with the principle of national treatment.[333]

This provision requires adjustments by China in two respects. First, China has to ensure non-discriminatory treatment of imported products in spite of the discriminatory treatment existing even in domestic products. Second, the discriminatory treatment, no matter how it is provided in regulatory documents in any form, or *de facto* affects imported products

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331 US Trade Representative, 'US-China Trade Relations: Entering a New Phase of Greater Accountability and Enforcement, Top-to-Bottom Review', February 2006.

332 US Trade Representative, 'US-China Trade Relations: Entering a New Phase of Greater Accountability and Enforcement, Top-to-Bottom Review', February 2006.

333 Para. 20, *Report of the Working Party on the Accession of China,* World Trade Organization 2001.

in practice, must be eliminated. These requirements attempt to bypass China's institutional difficulties by demanding adjustments in the treatment of imported products only. In other words, there is an expectation that a separate 'green channel' could be established, within the fragmented Chinese market, for imported products. This expectation manifests the WTO working party's dilemma with regard to China's accession. On the one hand, it recognizes that China's institutional problems may undermine the WTO trade liberalization goals. On the other hand, the limits of WTO jurisdiction mean it refrains from requiring institutional adjustments. The ineffectiveness of the central government's efforts to counter market fragmentation and enhance uniform administration show that the desired goal will be hard to achieve unless China makes changes in local protectionism and uniform administration as a whole. Foreign traders must be prepared for the possibility of local authorities adopting unexpected measures that may not be consistent with national rules.

In addition to Article III, China's commitments under the GATS are also hindered by the lack of a single market. China has committed, immediately after accession, to permit Chinese-foreign joint ventures and wholly foreign-owned enterprises to distribute their goods produced in China without being subject to any market access restrictions and with national treatment. Within three years after accession, it undertook to permit foreign service suppliers to provide both wholesale and retail services within China for all goods either produced in China or imported, through wholly foreign-owned enterprises or the joint ventures with minority or majority foreign ownership.[334] The market fragmentation problem results in a fragmented distribution network. An investigation conducted by the US found that China's distribution networks remained highly fragmented. There are no Chinese distribution companies with nationwide networks, and no Chinese distribution company has a market share greater than two per cent, due largely to limitations in infrastructure and restrictive provincial and local requirements.[335] As a result, the distribution rights committed to be provided to foreign service suppliers and foreign invested manufacturing enterprises cannot be guaranteed nationwide, and these suppliers and enterprises will probably encounter the same difficulties as domestic producers and distributors.

It is worthwhile clarifying whether China can invoke local protection rules as justification for violation of the WTO rules. As a general principle of international treaty law, a party to a treaty may not invoke the provisions of its internal laws as justification for its failure to perform a treaty obligation.[336] A special case applies if the issues concerned fall constitutionally outside the jurisdiction of the central/federal government. For this special case, Article XXIV:12 GATT adds an important provision. It stipulates that each member 'shall take such reasonable

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334 Protocol on the Accession of the People's Republic of China, Annex 9, Schedule of Specific Commitments on Services, Sector 4: Distribution Services.

335 US Trade Representative, '2005 Report to Congress on China's WTO Compliance', 11 December 2005.

336 WT/DS23/R, 39S/206, 296, para. 5.79, 19 June 1992; *Guide to GATT Law and Practice*, World Trade Organization 1995, p. 832.

measures as may be available to it to ensure observance of the provisions of this Agreement by the regional and local government and authorities within its territories'. According to the drafting history and the interpretation, this provision was designed to apply only to regional or local activities that were outside the control of the central government because of falling outside the jurisdiction of the central government under the constitutional distribution of powers.[337] That is to say, this provision grants a special right to central/federal states to take reasonable measures in respect of local activities in which they do not have constitutional jurisdiction, in order to ensure local governments' observance of the GATT. Therefore, China, where the central government is traditionally and constitutionally able to control the local governments, is obliged to ensure observance of the GATT by its local authorities and shall not invoke local rules as justification for violation of the WTO rules. Article XXIV:12 GATT should be regarded as an additional guarantee for the uniform administration requirement to be observed by the WTO members.

## 3.4 CONCLUSION

In a nutshell, China's compliance with the uniform administration requirement is impeded by the fragmented nature of its administrative and legal system. The decentralization reform in China over the past two decades has increased local autonomy and decreased the central government's control of local authorities, thus undermining the central government's ability to govern and leading to major difficulties in uniform administration of the application of law at local levels. The fragmented Chinese legal system, especially the inconsistency of the implementation of its laws, further exacerbates these difficulties. For the sake of its own regulation, the Chinese central government has made various *ad hoc* legislative efforts to eliminate local fragmenting measures and enhance uniform administration. However, the central legislation has not been effectively enforced at local levels and has thus failed to put an end to local trade barriers. Although the formulation of market fragmentation can be attributed to various factors, the continuance of the market fragmentation, after the central authority's legislative efforts to eliminate fragmenting measures, clearly demonstrates the central government's inability to achieve uniform administration of the implementation of central laws.

The study of market fragmentation highlights a tension facing the Chinese central government: how to continue promoting economic growth through the decentralization reform, while at the same time maintaining the effectiveness of laws and regulations as an institutional mechanism for state regulation. Interestingly, China's WTO membership has exacerbated the tension between local economic growth and national regulation by creating two opposite forces. On the one hand, the WTO requires further decentralization

337 WT/DS23/R, 39S/206, 296, para. 5.79, 19 June 1992; *Guide to GATT Law and Practice*, World Trade Organization 1995, p. 832.

of many economic activities to local government (foreign investment, for instance) to be compliant with WTO rules; on the other hand, the WTO requires centralization of the central government in order to ensure uniform administration of the application of trade rules at local levels. In this regard, a paradox has been created: the WTO needs China because of its fast economic development, which is largely attributed to the decentralization reform. However, this decentralization undermines China's ability to ensure uniform administration of the application of laws within its territory, and accordingly undermines the effectiveness of the WTO rules in China.

The importance of Article X:3(a) on uniform administration has been highlighted in this chapter. It is increasingly clear that this Article is not merely a conceptual due process requirement, but an essential guarantee for the effectiveness of substantive WTO trade liberalization obligations. China's case demonstrates that the deficiency of uniform administration makes it impossible for the WTO to review trade measures on the basis of non-discrimination rules and essentially makes the rule of national treatment a dead letter. Under the WTO adjunctive bodies' current interpretations, it is extremely difficult to establish a violation of Article X:3(a) if a 'pattern', not just a single case, of non-uniform administration has to be shown. Obtaining evidence is an especially challenging task as administrative acts are very much fact-based, and transparency levels in a country such as China are quite limited. There has not yet been a complaint against China as regards the violation of this Article. Considering, however, the direct impact that lack of uniform administration in China can have on the effectiveness of national treatment, the DSB should be prepared for future complaints, and at the same time reconsider the interpretation and application of this Article in order to allow it to contribute more effectively to achieving its main aim of ensuring the effectiveness of substantive WTO rules at national levels.

# Chapter 4

## Compliance with the Requirement of Judicial Review on Administrative Actions

## 4.1 INTRODUCTION

In order to enhance uniform implementation of laws by allowing individuals to challenge administrative decisions at domestic levels, Article X:3(b) GATT also requires members to maintain or institute judicial, arbitral or administrative tribunals or procedures for the prompt review of administrative actions relating to customs matters. Similar review obligations can be found in various WTO agreements, including the agreements on trade in goods, services, and intellectual property rights. These obligations represent internationally agreed minimum standards of procedural fairness which members are bound to implement in their domestic legislation. While the dispute settlement and trade policy review mechanisms provided by the WTO at an international level can only be initiated by governments of the member states, judicial review instituted at a domestic level provides an opportunity for individuals to claim their rights, thus ensuring uniform implementation of laws and constituting an extra legal safeguard for foreign traders. Those who disagree with administrative decisions can file their complaints to local courts for an independent judicial review.

China's WTO commitment on independent judicial review derives from a key provision of the Accession Protocol, which specifies that China shall establish tribunals and procedures for the prompt review of all administrative actions relating to the implementation of laws, regulations, judicial decisions and administrative rulings of general application referred to in Article X:1 of the GATT 1994, Article VI of the GATS and the relevant provisions in the TRIPS Agreement. This obligation is highly intrusive in respect of the domestic legal system and poses a serious challenge to China's judicial system. As a legal concept originating from Western countries, judicial review, as well as the philosophical and institutional foundations it develops upon, finds little resonance in Chinese history. It was introduced into China in the beginning of the last century, but was soon aborted because of the change of political regime. China's existing judicial review system has been under unfledged development for less than twenty years. Its characteristics are largely defined by China's unique historical, legal and institutional conditions. The features of China's indigenous conditions may restrict the role that judicial review can play in the correction of administrative actions. This chapter discusses how these indigenous conditions hinder effectiveness of judicial review in China, as well as China's efforts to improve judicial review in its foreign trade regime in order to be WTO-compliant. Part I briefly reviews the provisions and importance of judicial review in the WTO agreements, and the commitments undertaken by China. Part II examines Chinese legal traditions and the development of judicial review, while also introducing the contemporary judicial review system and its main legislation and practices. Part III analyzes the major obstacles existing in China's judicial review and demonstrates, through case studies, how these obstacles undermine the effectiveness of judicial review in practice. It also explains the impact that the lack of effective judicial review has on uniform legal application. Part IV evaluates China's efforts to improve judicial review, specifically for foreign trade-related matters, and analyzes whether these offer a feasible solution for making China more

compliant with the WTO requirements without any major institutional adjustments. Part V concludes the chapter and provides some prospects for future reform.

## 4.2 WTO REQUIREMENTS ON JUDICIAL REVIEW AND CHINA'S COMMITMENTS

### 4.2.1 Judicial Review Requirements in the WTO

Judicial review is often seen as a corollary of the very essence of the rule of law.[338] WTO law has incorporated this domestic legal concept into a total of twelve WTO agreements,[339] covering administrative actions in various aspects of trade, such as trade in goods, anti-dumping measures, technical barriers to trade, trade in intellectual property rights and trade in services.

The earliest provision requiring review procedures was contained in Article X:3(b) of the GATT 1947, which has since been carried over into the GATT 1994. It stipulates that:

> Each contracting party shall maintain, or institute as soon as practicable, judicial, arbitral or administrative tribunals or procedures for the purpose, inter alia, of the prompt review and correction of administrative action relating to customs matters. Such tribunals or procedures shall be independent of the agencies entrusted with administrative enforcement.

This provision imposes requirements on members' reviewing organs in two respects: the forms of reviewing organs, which can be judicial, arbitral or administrative, and the independent nature of review tribunals. The provisions in the TRIPS Agreement differ slightly from this provision. Article 41(4) of the *General Obligations* of *Enforcement of*

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338 Monica Claes, 'Judicial Review in the European Communities: the Division of Labour between the Court of Justice and National Courts', in Rob Bakker, Aalt Willem Heringa, Frits Stroink (ed.), *Judicial Control-Comparative Essays on Judicial Review*, Maklu Uitgevers Antwerp-Apeldoorn, 1995; Michael Palmer, 'Controlling the State?: Mediation in Administrative Litigation in the People's Republic of China', *Transnational Law and Contemporary Problems*, Autumn 2006.

339 1) Article X:3(b) of GATT 1994; 2) Article 13, Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-Dumping Agreement); 3) Article 23, Agreement on Subsidies and Countervailing Measures; 4) Article 3, para. 5(e), Agreement on Import Licensing Procedures; 5) Annex C, para. 1(i), Agreement on Sanitary and Phytosanitary Measures; 6) Article 5.2.8, Agreement on Technical Barriers to Trade; 7) Article XX (6), Agreement on Government Procurement; 8) Article 4, Agreement on Preshipment Inspection; 9) Article 11(1) and (2), Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 (Custom Valuation Agreement); 10) Articles 2(j) and 3(h), Agreement on Rules of Origin; 11) Article VI, para. 2, General Agreement on Trade in Services (GATS); 12) Article 31(i) and (j), Article 32, Article 41, para. 4, and Article 62, para. 5, Agreement on Trade-related Aspects of Intellectual Property Rights.

*Intellectual Property Rights* provides, for example, that 'Parties to a proceeding shall have an opportunity for review by a judicial authority of final administrative decisions'. It restricts the form of the reviewing organ to a judicial organ. Despite the different requirements for the forms of the tribunal, the TRIPS Agreement also emphasizes the independent nature of the review tribunal.[340] In this regard, however, the GATS seems to provide for a less restrictive requirement. It states that 'when review procedures are not independent of the agency entrusted with the administrative decision concerned, the member shall ensure that the procedures in fact provide for an objective and impartial review'.[341]

In fact, there is no uniform requirement as regards the review procedures in WTO law. The judicial review requirement contained in different trade agreements enjoys its own characteristics and varies in certain respects, including in the form of review tribunal, the extent of independence and the scope of review. However, the critical requirement is not the form or the scope of the review. Rather it is the independent nature of the review that decides whether an objective and impartial review can be provided to protect individual rights against administrative decisions and thereby ensure fulfillment of the WTO rules more effectively at the national level.

The importance of the judicial review requirements in the WTO lies in three aspects. Firstly, it is essential for the uniform implementation of the WTO commitments. WTO agreements are mainly implemented by domestic administrative agencies adopting trade policies or measures. The judicial review requirement, however, requires domestic judicial organs to intervene in the implementation process by reviewing administrative actions and correcting inconsistent ones. While the WTO has two procedures (the TPRM and DSS) for supervising members' implementation at an international level, the judicial review requirements constitute a specifically domestic procedure to ensure conformity of national laws and implementation in accordance with the WTO obligations.

Secondly, it has crucial implications for good governance and due process, thereby promoting the rule of law purported by the WTO. Through objective and impartial review, it helps to ensure that every actor in the society, including ordinary citizens, the government and its officials, is subject to the rule of law.

Thirdly, it provides a direct remedy for individual traders to challenge inconsistent practices of member governments at domestic levels. This function is of particular importance in the WTO legal system as it provides indirect protection of individual rights. The WTO

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340 TRIPS Agreement Article 31 '*Other Use without Authorization of the Right Holder*' under the *Section of Patent*: (i) the legal validity of any decision relating to the authorization of such use shall be subject to judicial review or other independent review by a distinct higher authority in the Member.

341 GATS Agreement Article VI 2(a).

agreements comprise a system of obligations and rights for member governments.[342] None of these obligations applies directly to individual actors.[343] Individuals do not acquire substantive rights directly from WTO agreements, but instead indirectly from governments' implementation of the WTO obligations. If a government fails to fulfill the WTO requirements and infringes individual rights, aggrieved individuals should enjoy a procedural right to challenge the government's actions. However, under the DSS, only member governments can initiate complaints to the WTO. Since the protection of individual rights is quite indirect under the mechanism provided by the WTO at an international level, more direct protection of individual rights is needed at a domestic level. In this regard, a judicial review system in every member constitutes an indispensable mechanism for individuals to challenge incompliant practices of a government. As individuals can observe inconsistent practices during their daily economic activities, the judicial review mechanism can ensure more effective observance of WTO obligations and assist individual traders in gaining more benefits from the WTO agreements.

### 4.2.2 China's Commitments

In Article 2 (D) of the Accession Protocol of China, China undertook to:

> [E]stablish, or designate and maintain tribunals, contact points and procedures for the prompt review of all administrative actions relating to the implementation of laws, regulations, judicial decisions and administrative rulings of general application referred to in Article X:1 of the GATT 1994, Article VI of the GATS and the relevant provisions of the TRIPS Agreement. Such tribunals shall be impartial and independent of the agency with administrative enforcement and shall not have any substantial interest in the outcome of the matter.

Under this commitment, China shall establish a judicial review of administrative actions relating to the implementation of law or regulations in trade in goods and services as well as trade relating to intellectual property rights. As provided in Article X:1 of the GATT, the laws or regulations and their implementation that shall be reviewed under China's commitments include 'laws, regulations, judicial decisions and administrative rulings of general application, pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges, or to requirements, restrictions or prohibitions on imports or exports or on the transfer of payments, or affecting their sale, distribution, transportation, insurance, warehousing inspection, exhibition, processing, mixing or other use'. Compared with the provision in Article X: 3 of the GATT, which requires judicial review only for customs matters, China's commitments expand the scope of judicial review in all trade-related areas, thus making it broader than the requirement of Article X:3(b). In the report of the

342 Steve Charnovitz, 'The WTO and the Rights of the Individual', *Intereconomics*, May/April, 2001.

343 Steve Charnovitz, 2001.

working party, China also confirmed that the tribunals responsible for such reviews would be impartial and independent of the agency responsible for administrative enforcement.[344]

## 4.3 JUDICIAL REVIEW IN CHINA – DEVELOPMENT, LEGISLATION AND PRACTICES

Judicial review, which has existed for a long time in Western countries, is nascent to China. It was virtually non-existent until the early 20th century, when Western political and economic ideas started penetrating into China.[345] China introduced its first legislation on judicial review in 1989. It was one of the products of China's contemporary legal reform that has been characterized as a process of learning from China's past and from other countries' experience.[346] Although mainly modeled on foreign legal systems, the unique historical, cultural and political background of China means its judicial review has developed its own characteristics.[347] The context of its development, as well as the way in which it differs from judicial review in Western countries, contributes to the understanding of China's current judicial review system.

### 4.3.1 Basic Concept of Judicial Review in the Western Context

Since the WTO agreements do not provide an explicit explanation of judicial review, we have to refer to its definition in the Western context, where judicial review is commonly considered to be conceived and developed. It is generally agreed that judicial review means a power exercised by the courts and that provides checks on other branches so as to keep their powers within the limits of the constitutions or their delegated authorities.[348] More accurately, Justice Robert F. Utter and David Lundsgaard define judicial review as 'a judicial action that involves the review of an inferior legal norm for conformity with a higher one,

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344 Report of Working Party of China's accession, paras. 76-79.

345 In 1914, Yuan Shikai government established a Court of Administrative Justice, which was authorized to hear cases involving unlawful administrative actions. It was deemed the first step of judicial review in China. However, due to the unstable political environment, few people knew that Court of Administrative Justice existed. The second law concerning judicial review was issued in 1932 by the Nationalist government. After the founding of the PRC in 1949, the new government abolished all the fundamental laws of the Nationalist regime, including the law on judicial review. Susan Finder, 'Like Throwing An Egg Against A Stone? Administrative Litigation in the People's Republic of China', *Journal of Chinese Law*, 1 June, 1989.

346 Pitman B. Potter, *The Chinese Legal System:Globalization and Local Legal Culture*, Routledge Curzon, 2002. As regards how China learned from foreign experience in reconstructing its own legislation.

347 China's existing law on judicial review (Administrative Litigation Law) is heavily influenced by US Federal Administrative Procedure Act.

348 Kathleen M. Sullivan and Gerald Gunther, *Constitutional Law*, Foundation Press, 14th edition, 2001, p. 13. See also Oxford Law Dictionary, edited by Elizabeth A. Martin and Jonathan Law, Sixth Edition, Oxford University Press.

with the implicit possibility that the reviewing court may invalidate or suspend the inferior norm if necessary or desirable'.[349] It 'includes review of legislatively enacted statutes as well as review of administrative and executive decrees for compliance with constitutional principles'.[350] It also includes 'the practice of reviewing administrative and executive actions for compatibility with controlling statutes'.[351] As reflected by this definition, the scope of judicial review can generally refer to a constitutional judicial review (i.e. a constitutionality check of legislative or executive actions) and an administrative judicial review (i.e. a review of the legality of administrative actions). The scope of judicial review includes not only laws and administrative decrees with general binding force, but also specific administrative actions adopted in respect of individuals or legal persons.

There are many variables affecting judicial review in different nations, such as the history and traditions of a country, its particular demands and aspirations, and its political and legal structures. Across the world, judicial review has developed in two main directions: one based on the US common law system and one based on the civil law system of continental Europe.[352] In the United States, constitutional and administrative judicial reviews are both exercised by the ordinary judiciary. There is no specific court with monopolistic jurisdiction to exercise only constitutional review.[353] Constitutional litigation in the United States does not have a different status from other forms of litigation.[354] The European continental model is based on the principle of legislative supremacy; in other words, it is the legislator's responsibility to decide whether a bill is in accordance with the Constitution. In most European countries, ordinary courts do not have the power to review the constitutionality of primary legislation. The power of constitutional review lies in special courts, such as the Constitutional Court in Germany, or in the government and the Parliament in the Netherlands. In the Netherlands, courts are not allowed to review the constitutionality of formal laws (laws of parliament).[355] Constitutionality checks are conducted during the preparatory stage of laws by the bodies involved in enacting legislation (i.e. the Council of State in its advisory role, and the legislature; in other words, the government and both

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349 Robert F. Utter and David C. Lundsgaard, 'Judicial Review in the New Notions of Central and Eastern Europe: Some Thoughts from a Comparative Perspective', *Ohio State Law Journal*, No. 54, 1993.

350 Robert F. Utter and David C. Lundsgaard, 1993.

351 Robert F. Utter and David C. Lundsgaard, 1993.

352 Gustavo Fernandes de Andrade, 'Comparative Constitutional Law: Judicial Review', *University of Pennsylvania Journal of Constitutional Law*, No. 3, 2001. Most European countries' judicial review systems fall within this one, except the UK and the Netherlands. The practice of judicial review in the European Court of Justice is quite different from the general practice applying in continental Europe.

353 Stephen R. Alton, 'From Marbury v. Madison to Bush v. Gore: 200 Years of Judicial Review in the United States', Texas Wesleyan Law Review, No. 8, 2001.

354 Stephen R. Alton, 2001.

355 Article 120 of the Constitution of the Netherlands. Although courts are not allowed to review whether formal laws are in accordance with the Constitution, they are allowed to (and must) check whether formal laws are in accordance with treaties and decisions of international public bodies such as the European Union; see Article 94 of the Constitution of the Netherlands.

Houses of Parliament). Although forbidden from constitutionality checks on formal laws, Dutch courts are allowed to review the constitutionality of material laws, which are next to formal laws and are issued by lower bodies.

Despite the differences between the two models of judicial review, the reviewing body – whether it is a constitutional court or otherwise – is independent of the body being reviewed. This guarantees effective checks on other branches of the government in order to control the legality of their actions and protect individual rights. As to the scope of judicial review in both forms, the review body includes constitutional judicial review and administrative review, irrespective of whether it is an ordinary or special court. This means that not only can specific actions and measures be challenged, but so, too, can the regulations, acts, or laws that enable the authority to take such actions or measures.

The fundamental principle behind the development of judicial review is the concept of the rule of law.[356] The concept of the rule of law is based on the principle that all powers of public bodies originate from and are at the same time limited by the law.[357] According to this concept, the law is not only the instrument whereby characteristics of its bodies and officials are established, but also the instrument limiting the exercise of those characteristics.[358] Consequently, a state operating in accordance with the rule of law is essentially a state with limited powers and subject to a form of judicial control.[359] In essence, judicial review is concerned with the relationship between three main branches of the state. It is all about the checks and balances exercised by the judiciary over the other branches, executive or legislative, of the state. Judicial review is also an important judicial procedure for resolving disputes relating to public administration so as to protect the legitimate rights and interests of citizens, legal persons and other organizations. Under this legal institution, a citizen, legal person or other organization whose legitimate rights or interests have been infringed by administrative actions is entitled to turn to the court for a judicial remedy.

Judicial review embodies three main features of the rule of law: the separation of powers, the submission of the state to law, and the establishment of a set of fundamental rights and liberties.[360] Under a judicial review system, administrative acts and decisions are invalid if

356 Richard E. Levy and Sidney A. Shapiro, 'A Standard-Based Theory of Judicial Review and the Rule of Law', *Wake Forest University Legal Studies Paper* No. 05-16, July 2005; Bradley Selway QC, 'The Principles behind Common Law Judicial Review of Administrative Action – The Search Continues', *Federal Law Review*, issue 8, 2002; Louis Jaffe and Edith Henderson, 'Judicial Review and Rule of Law: Historical Origins', 72 *Law Quarterly Review* 345, 1965; Allan R. Brewer-Carias, *Judicial Review in Comparative Law*, Cambridge University Press, 1989; Ian McLeod summarized three fundamental doctrines of British judicial review: the legislative supremacy of Parliament, the rule of law and the separation of powers, in *Judicial Review*, published by Barry Rose Law Publishers, Second edition, 2001, pp. 10-14.

357 Allan R. Brewer-Carias, 1989, p. 7.

358 Allan R. Brewer-Carias,1989, p. 7.

359 Allan R. Brewer-Carias, 1989, p. 7.

360 Allan R. Brewer-Carias, 1989, p. 80.

they are in breach of or unauthorized by the law, or beyond the scope of the power given to the decision maker by the law.[361] The power of review conferred on judicial organs demonstrates the strict separation of legislative, administrative and judicial organs, as well as numerous checks and balances.

Thus, the principles behind judicial review as developed in the Western context can be summarized as the rule of law, the separation of powers in a state structure, the protection of fundamental rights and liberty of individuals, and the supremacy of the Constitution. All modern Western constitutions provide for some form of judicial control of state actions by independent courts, even though the extent to which this judicial control can be exercised is not equal in all states.[362]

## 4.3.2 Evolution of Judicial Review in China

### *4.3.2.1 Chinese Legal Tradition and Culture – Legitimacy of Judicial Review*

Law in any socialist country bears the birthmark of the country's own history, culture, and tradition.[363] Legal culture can be viewed as an internal logic by which the law and the way it is enforced in a society can be understood.[364] The post-Mao law reforms in China placed heavy reliance on imported legal norms, and foreign influences are extensive in the country's legislature and legal institutions.[365] Although foreign influences make many Chinese laws and institutions appear recognizable to Western legal scholars, the norms and practices of these laws often depart quite significantly from the expectations of those familiar with liberal legal

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361 Allan R. Brewer-Carias, 1989, p. 80.

362 Some countries operate a narrow judicial review, prohibiting judicial review on constitutionality. Article 120 of the Dutch Constitution 1983 states, for example, that judges are not allowed to check laws and treaties for their constitutionality. Constitutionality checks are conducted by the legislator, not by the judiciary. Monica Claes, 1995.

363 Xin Ren, 'Tradition of the Law and Law of the Tradition – Law, State, and Social Control in China', Greenwood Press, 1997, p. 4.

364 Merryman, J.H., 'The Convergence (and Divergence) of the Civil Law and Common Law', in M. Cappeletti (ed.), New Perspectives for a Common Law of Europe, Sijthoff Publishing Co., 1978, pp. 222-227.

365 Legal reformers in the legal reforms undertaken since 1978 were instructed to learn from China's past and the experience of foreign countries. The drafting of the 1978 Criminal Law, the Criminal Procedure Law, and the Organizational Law of the People's Court relied primarily on prior drafts and enactments from the 1950s, which had been based largely on Soviet models. The General Principles of Civil Law (1986) were based on relatively well-developed drafts begun during the 1950s and continued during the post-Mao period, which themselves were derived from the European and Soviet experience. As the economic reforms accelerated, China's legal specialists looked increasingly to Europe and North American for inspiration. During the 1980s, legislation on such matters as environmental protection, regulation of foreign and domestic business, intellectual property, civil procedure and arbitration drew increasingly on European and North American models.

systems.[366] The foreign influences have largely been limited to the structures, organization and content of laws, but have had little effect on the basic normative premises underlying the operation of China's legal system. It is the local legal culture that determines which elements of and to what extent a foreign legal tradition can be assimilated into the Chinese legal system and subsequently transformed into social reality in Chinese society. Traditional norms provide a context in which the norms of contemporary China's legal culture operate.

Despite the fact that the existing Administrative Litigation Law of China (ALL) was heavily influenced by the US Federal Administrative Procedure Act, the principles and philosophical ideals behind judicial review in Western countries seem to find little resonance in Chinese traditional culture.[367] In the Western context, according to Locke, the relationship between individuals and political society is based on an agreement, under which fundamental rights or natural rights of individuals are recognized in the Constitution, and these rights are beyond the power of government.[368] Constitutionality checks are instituted in order to ensure that the fundamental rights of citizens are not infringed by actions of governments. Chinese legal tradition, by contrast, is based on a completely different philosophical ideal. Rulers had divine powers, and all rights of individuals were granted by rules.[369] Under this top-down power system, the arbitrary power of government was rarely limited, or more precisely, had no grounds to be limited by anything beyond the government itself.[370] Except for criminal sentences, all behavior of officials and actions of governmental organs were controlled by internal censorship within the administrative system,[371] and this self-supervised administrative model is reflected in the contemporary administration of China.

There are two features in China's traditional legal system and state structure that largely determine the form of the judicial review system. Firstly, all powers were highly centralized

366 For detailed discussions, see Pitman B. Potter, '*The Chinese Legal System*', Routledge Press, 2001, pp. 17-37; Xin Ren, 1997, pp. 2-3.

367 M. Ulric Killion refers to the words of Samuel P. Huntington, who wrote that 'Western ideas of individualism, liberalism, constitutionalism, human rights, equality, liberty, the rule of law, democracy, free markets, the separation of church and state, often have little resonance in Islamic, Confucian, Japanese, Hindu, Buddhist or Orthodox cultures'. M. Ulric Killion, 'Post-WTO China and Independent Judicial Review', 26 *Hous. J. Int'l. L.*, p. 507, 2003-2004.

368 Allan R. Brewer-Carias, 1989.

369 Xiaofeng Chen summarized that the source of power in the West originates from a bottom-to-top pattern: 'property rights-individual rights-power of government'. In China, the power source pattern is top-to-bottom: 'power of government-individual rights-property rights'. Xiaofeng Chen, *Studies on Chinese Legal Culture*, Henan People's Publishing House, 1993, p. 33.

370 Xiaofeng Chen, 1993, p. 33.

371 According to Chinese legal tradition, with the exception of criminal sentences, the administration of actions of officials, no matter whether they are individual actions or duty actions, was implemented by an administrative organ called '*Libu*' (board of administration of officials 吏部). This censorial institution had the power and duty to watch, scrutinize, and criticize the conduct of all members of the officialdom.

in a ruler; this resulted in law having only a limited role.[372] The theory of the separation of powers was wholly unknown in traditional Chinese legal culture.[373] The emperor was enthroned as the son of heaven by the orthodox theory of feudalism and by military powers.[374] The emperor's power emanated from nature *(junquan shenshou*), and any utterance of the emperor was taken as law (*fazi junchu*). From the Chinese point of view, the central element of their legal system was a body of rules promulgated by the emperor. The formal legal system was an integral part of the governing apparatus of the empire. As a result, the emperor/ruler was immune from any legal obligation and could not be regulated by law.[375] The purpose of the law was to guide people's conduct so as to create a harmonious social order. That is to say, the object of the law was primarily deterrent and not retributive.[376] Laws were means of authoritarian government rather than democratic government insofar as the source of legislation was in the hands of the emperor, and the law was a model or standard not set up by the people themselves, but imposed from above and to which the people had to conform.[377]

Historically law was a tool used by the ruler to regulate the ruled,[378] and this instrumentalism of law has continued to apply under the socialist legal system. The most obvious feature of traditional Chinese society was the emphasis on hierarchy. In feudal China, social order was not primarily sustained by law, but instead by ethics dictated by patriarchal authority and requiring absolute obedience of the inferior to the superior. The most dominant ideology in traditional China was Confucianism, which favors achieving social harmony through moral persuasion. Although elements of the legalist tradition were retained in imperial China after the Han Dynasty, these tended to focus on the severity of criminal punishment rather than on the objectivity and universality of the legalist concept of *fa* (law).[379] The Confucian concept of *li* (propriety) dominated the regulation of social relationships and held these to be inherently unequal.[380] Such inequality, and the hierarchical social structures that resulted, was deemed essential to the orderly existence of society.[381] Thus, there did not emerge a natural rights tradition that might have served as a basis for demands of equality.[382]

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372 Xiaoxin Ye, *Chinese Legal History*, Peking University Press, first printed in 1996, and reprinted in 1999. This book was selected as a textbook for law school students in many Chinese universities during the period 1997-2002.

373 Anthony R. Dicks, 'Compartmentalized Law and Judicial Restraint: An Inductive View of Some Jurisdictional Barriers to Reform', *The China Quarterly*, No. 141, 1995.

374 Wang Chenguang and Zhang Xianchu, *Introduction to Chinese Law*, Sweet & Maxwell Asia, 1997, p. 5.

375 Xiaoxin Ye,1999, pp. 2-3.

376 Hyung I. Kim, *Fundamental Legal Concepts of China and the West – A Comparative Study*, Kennikat Press, 1981, p. 17.

377 Hyung I. Kim, p. 17.

378 Xiaoxin Ye,1999, p. 3.

379 Pitman B. Potter, *The Chinese Legal System – Globalization and Local Legal Culture*, 2001, p. 8.

380 Pitman B. Potter, *The Chinese Legal System – Globalization and Local Legal Culture*, 2001, p. 8.

381 Pitman B. Potter, *The Chinese Legal System – Globalization and Local Legal Culture*, 2001, p. 8.

382 Pitman B. Potter, *The Chinese Legal System – Globalization and Local Legal Culture*, 2001, p. 8.

Moreover, human relations in China were essentially clan relations; hence there was no real subscription to the principle of universality.[383] Within this compelling context, law became an extension of hierarchical norms, and this reinforced hierarchy and obligations rather than a notion of rights as separate from obligations.[384] The Qing Code, which was at the heart of the Qing Dynasty, for example, was a collection of rules predominantly concerned with the official activities and functions of the bureaucrats within the government apparatus, not with disputes and relationships between and among private citizens. William Jones' study of the Qing legal code concluded that law was designed to protect the interests of the imperial state and could not conceive of legal relations between citizens.[385] For individuals, 'law' was perceived as essentially punitive, or criminal in nature. There was no social reinforcement to encourage individuals to pursue rights. Involvement in lawsuits was inconsistent with social mores stressing the importance of harmony, while a psychological fear of punishment prompted people to avoid lawsuits and to seek communal mediation outside the law.[386] This legal culture may explain the generally hostile attitude toward litigation, especially litigation against government or administrative agencies. This hesitation continues to exist to a certain extent in contemporary China.[387]

Secondly, the judiciary and administration were inseparable. Judicial organs have been subordinated to administrative agencies throughout Chinese legal history.[388] At least since the Tang Dynasty and until the end of Qing in 1911, the system of government in China consisted of a strong central government headed by the emperor, who ruled through a bureaucracy and with absolute power.[389] The lowest ranking officials represented the central government at the county level and in effect exercised all the power of the state, including tax collection, public works, and even deciding lawsuits.[390] Thus, adjudication was simply one of the many administrative duties of a government official, who adjudicated cases at the local level, but was not a judge as we understand the term.

In the Tang Dynasty, for example,[391] the highest administrative agency was Shangshu Department (*Shangshu Sheng*) at the central level, under which 'six boards' (*liubu*) were

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383 Ronald C. Keith, *China's Struggle for the Rule of Law*, St. Martin's Press, 1994, p. 48.

384 Ronald C. Keith,1994, p. 48.

385 Willing C. Jones, 'Studying the Ch'ing Code – The Ta-Ch'ing Lu Li', *The American Journal of International Law*, vol. 22, 1974, p. 356.

386 See Ronald C. Keith,1994, pp. 48-49.

387 Wang Chenguang and Zhang Xianchu,1997, p. 6.

388 Xiaoxin Ye,1999; Xiaofeng Chen,1993.

389 William C. Jones, 'Trying to Understand the Current Chinese Legal System', in C. Stephen Hsu (ed.), *Understanding China's Legal System: Essays in Honor of Jerome A. Cohen,* New York University Press, 2003; Zhuwu Chen, 'Capital Market and Legal Development: the China Case', *China Economic Review*, vol. 14, issue 4, 2003.

390 William C. Jones, 2003; Xiaoxin Ye,1999, p. 222.

391 The legal system in the Tang Dynasty was comparatively more completed and sophisticated. Xiaoxin Ye,1999, p.222.

established, based on six different subject matters of jurisdiction.[392] Among these boards, the *Xingbu* (Board of Punishment) was the judicial organ with adjudication power.[393] Under these institutional arrangements, the judicial organ existed as one of the branches under the highest administrative agency. At the central level, the chiefs of administrative agencies were able to interfere in the judiciary; however, the chief of judiciary could not interfere in the administration.[394] No separate judicial organs were ever established at the local level.[395] The chief administrative official was the highest local governor, who exercised both the power of administration and the power of adjudication.[396] As a result, the judicial function became an annex or branch of the administrative authorities. It is thus not difficult to recognize that the problem of non- independent judiciary in contemporary China, particularly at local levels, has its roots in the country's history. As far as the community at large is concerned, judges and administrative officials are all governmental officials, and this explains why people are reluctant to sue administrative authorities.

#### *4.3.2.2 Development of Regulation of Administrative Actions after 1949*

By the late 19th century, the traditional legal system was facing strong challenges and pressure for reform both from outside and inside. Internally, a commodity economy had emerged, while externally Western economic, cultural and political ideas had penetrated into China.[397] In May 1914, Yuan Shikai's government issued the law governing administrative litigation.[398] In 1932 the Nationalist government promulgated a second law establishing an Administrative Court and administrative litigation procedure.[399] However, the impact of the Court was very limited[400] as it could not award damages, and most citizens were either unaware of its existence or did not have the resources to make the necessary appeals.[401] Due to the prevailing political conditions, including civil war and Japanese occupation, the Court was rarely used.[402] Prior to 1949, therefore, the incipient administrative litigation system had no significant impact.

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392 The six boards consisted of *Libu* (board of administration of officials 吏部), *Hubu* (board of finance户部), *Libu* (board of rites礼部), *Bingbu* (board of military兵部), *Xingbu* (board of punishment and judiciary刑部) and *Gongbu* (board of works工部, including construction, irrigation, agriculture and fisheries). See Xiaoxin Ye, *Chinese Legal History*, Peking University Press, first printed in 1996, and reprinted in 1999, p. 207.

393 Xiaoxin Ye,1999, p. 207.

394 Xiaoxin Ye, 1999, p. 4.

395 Xiaoxin Ye, 1999, p. 4.

396 Xiaoxin Ye, 1999, p. 4.

397 J. Chen, *Chinese Law-Towards an Understanding of Chinese Law, Its Nature and Development*, Kluwer Law International, 1999, p. 129.

398 J. Chen, 1999, p. 130.

399 Susan Finder,1989.

400 Susan Finder, 1989.

401 Susan Finder, 1989.

402 Susan Finder, 1989.

After the founding of the PRC in 1949, the new leaders abolished the fundamental laws of the Nationalist regime, including the legislation of administrative litigation.[403] Efforts to establish a socialist legal system were actively undertaken in the early days of the PRC. Between 1949 and 1956, many laws dealing with state administration were issued.[404] The first formal Constitution of the PRC, in 1954, stated, for example, that citizens had the right to bring complaints alleging a transgression of law against any person working in an organ of state.[405] That legislation, however, was terminated by a series of political movements that started in the late 1950s. As a result, the extent to which rudimentary administrative litigation was developed in the early stages of the PRC was limited.

As discussed above, Chinese administrative law has developed in an essentially different way from in the West. In contrast to concepts such as checks and balances, the principle of *ultra vires* and control of power, Chinese administrative law emphasizes its function to secure smooth operation of state administration. Administrative activities should be governed mainly to ensure the validity and legality of state administration over the people.[406] There is little discussion about protecting individual rights against the abuse or misuse of government powers. Moreover, socialism exerts further influence on the administrative legal system through the assertion that the 'Chinese Communist Party (CCP) always represents the fundamental interests of overwhelming majority of the Chinese people'.[407] This assertion argues that the interests of the government and the people are essentially identical and there should be no fundamental conflict between them.[408] Thus, it is not surprising to see that supervision of administrative activities is largely based on internal review (self-supervision of administrative organs) rather than on external review (judicial review, for example).

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403 Common Program of the Chinese People's Political Consultative Conference, adopted on 29 September 1949. See also Susan Finder,1989.

404 J. Chen, 1999, p. 132.

405 Article 97 of the 1954 Constitution provided 'people suffering loss by reason of infringement by persons working in organs of state of their rights and citizens have the right to compensation'.

406 Pi Chunxi & Feng Jun, 'Some Considerations on the Loopholes in the Theory of Balance – The Direction for Improvement', *Legal Science in China* (Zhongguo Faxue), No. 2, 1997.

407 See the ideology of 'Three Represents', namely that the CCP always represent the development trend of China's advanced productive forces, the orientation of China's advanced culture and the fundamental interests of the overwhelming majority of Chinese peoples. It is a socio-political ideology credited to General Secretary Jiang Zemin and became a guiding ideology of the CCP at its Sixteenth Party Congress in 2002.

408 Jyh-Pin Fa and Shao-chuan Leng, 'Judicial Review of Administration in the People's Republic of China', *Case Western Reserve Journal of International Law,*,vol.23, issue.3, 1991; J. Chen, , p. 132.

There are several methods available for internal review of administrative activities.[409] One frequently used device is the 'Letters and Visits' (*xinfang*) system, which is seen as the CCP's own creation and still exists today. It enables citizens who disagree with administrative decisions to lodge a complaint at a 'Letters and Visits' office established to handle such matters within the relevant administrative body. Its function lies in two aspects: firstly it is regarded as a way to promote democracy since it encourages people to express their disagreement with state administration and supervises administrative activities to a certain extent; secondly it exists as a supplement to judicial remedy for administrative grievances. Many people, especially those from the countryside, regard visiting central 'Letters and Visits' office in Beijing as the most reliable and the ultimate resort if their rights fail to be protected effectively at the local level. This view derives from the traditional belief that more justice exists in the superior administration.

The popularity of the 'Letters and Visits' system reflects the continued belief that, as in imperial China, officials have a quasi-parental moral duty to correct bureaucratic wrongdoing and errors.[410] This quasi-parental character of government is seen in return as justifying the belief that there should be no fundamental conflict of interests between the government and the people, and thus any problem occurring in the process of state administration should be able to be resolved internally. Compared with administrative litigation, this model of complaint is non-confronting and does not bring with it the opprobrium of 'challenge [the] state'.[411] Although the 'Letters and Visits' system has been effective in improving communications between the government and the people, reliance on this single forum has left many problems in administrative acts unresolved.[412] Indeed the fact that many of the letters sent by citizens are anonymous demonstrates people's fear of retaliation and their cynicism toward the system.[413]

China has been implementing a program of legal reform since the late 1970s. The party leaders, especially Deng Xiaoping, realized that the major problem facing China was economic development.[414] Along with calls for economic modernization, the post-Mao

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409 For example, (i) Administration Reconsideration (*xingzheng fuyi*), which permits an aggrieved citizen to challenge an unsatisfactory decision by filing an application for review at the next superior level within the same branch of government. The procedures for administrative reconsideration are provided in the Administrative Reconsideration Law adopted in 1999; (ii) Administrative Supervision (this functions similarly to the ombudsman in Europe and North America), under which the Ministry of Supervision and its subordinate agencies bear responsibility for ensuring good standards of administration by state organs and their personnel; and (iii) the Letters and Visits system.

410 Michael Palmer, 2006.

411 Michael Palmer, 2006.

412 Jyh-Pin Fa and Shao-chuan Leng, 1991.

413 Jyh-Pin Fa and Shao-chuan Leng, 1991

414 Jianfu Chen, 'Market Economy and the Internationalization of Civil and Commercial Law in the People's Republic of China', in Kanishka Jayasuriya (ed.) *Law, Capitalism and Power in Asia*, Routledge, 1999, pp. 70-72.

Chinese leaders consequently devoted tremendous attention to re-establishing a legal system. What motivated Deng and his associates to make legal development a top priority as they tried to modernize the economy? As Shiping Zheng pithily summarized, there were perhaps four main reasons: revulsion against the Cultural Revolution; the need for new sources of legitimacy; concerns about social order and stability, and economic imperatives.[415] At the Third Plenary Session of the 11th Central Committee of the Communist Party of China, it was affirmed that 'In order to safeguard people's democracy, it is imperative to strengthen the socialist legal system so that democracy is systematized and written in such a way as to ensure the stability, continuity and full authority of this democratic system and the laws. There must be laws for people to follow, these laws must be observed, their enforcement must be strict and law breakers must be dealt with'.[416]

In order to keep pace with the rapid development of the economy, the legal reform has largely centered on efforts to enact new legislation in various areas, including administrative regulation. In addition to non-legal remedies, China has since the 1980s gradually taken steps toward legal redress in order to intensify the control and supervision of administrative acts. In 1982, the Civil Procedural Law for the first time provided for the right of judicial review of administrative activities.[417] The economic and civil divisions of the People's Court then began to accept judicial cases. This continued until early 1987, when the Supreme People's Court issued an order establishing, on an experimental basis, administrative divisions specializing in judicial review cases in People's Courts in various parts of the country[418]. In 1989, the Administrative Litigation Law (ALL) was passed; this was regarded as breakthrough legislation since it replaced the previous scattered provisions and finally established the institutional framework necessary to develop judicial review in China.

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415 Firstly, the initial impulse for restoring the legal order in the late 1970s came as a result of disgust caused by the chaos and mass violence of the Cultural Revolution. Most of the post-Mao leaders had been victims of Mao's abuse of power and had suffered in a lawless situation. The changing political climate was a second reason for reconstructing the legal system. After Mao died, it did not take the rehabilitated leaders long to realize that social support for the Party had greatly eroded. The new regime attempted to shift away from class struggle to a legal system as the new basis of legitimacy. The third reason for legal reform was that laws and regulations could help the new regime maintain social order and stability. Finally, there was an economic need for legal development. Laws and regulations were needed not only to secure a stable and orderly environment essential to the success of economic modernization, but also to regulate many new types of economic activities and relationships resulting from market reform and privatization. For a detailed discussion of how these four factors have affected China's decisions on legal reform, see Shiping Zheng, *Party vs. State in Post-1949 China – The Institutional Dilemma*, Cambridge University Press, 1997, pp. 162-166.

416 The Communiqué of the Third Plenum of the Eleventh Congress of the Chinese Communist Party, Beijing: Foreign Language Press, 1978.

417 Article 3 of the Civil Procedural Law of the People's Republic of China (Trail), issued on 8 March 1982 and which has since become invalid.

418 'Notice Concerning the Establishment of Administrative Adjudicative Divisions', issued by the Supreme People's Court, 14 January 1987.

### 4.3.3 Current Legislation of Judicial Review in China

The ALL allows Chinese citizens and organizations, as well as foreigners and foreign organizations, to initiate court proceedings against 'concrete administrative acts' which have allegedly infringed upon their rights.[419]

#### *Jurisdiction*

Basic courts have jurisdiction over most administrative litigation cases. Intermediate courts have jurisdiction over four specific types of cases: certain patent right cases, customs cases, major or complicated cases, and cases concerning national ministries and commissions, provincial governments and directly administered municipalities.[420] The Supreme People's Court may act as the court of first instance only in major or complicated cases that pertain to the entire nation.[421] All administrative litigation cases are handled by administrative divisions established under each court.[422]

#### *Scope of Judicial Review*

Not all administrative acts can be challenged under the ALL. The general principle is provided for in Article 2 of the ALL, which stipulates that courts can only accept lawsuits against *concrete administrative acts*. The reviewable *concrete administrative acts* are defined as unilateral administrative decisions on specific issues affecting a specific group of citizens, legal persons or other organizations.[423] Although the ALL does not provide a definition of concrete administrative acts, it contains a clause listing eight categories of administrative acts that can be reviewed by courts. For example, the refusal to accept an administrative sanction such as a detention, fine, rescission of a license or permit, order to suspend production or business or confiscation of property, or a compulsory administrative measure such as the refusal to accept a restriction on the freedom of a person or the sealing-up, seizing or freezing of property.[424] The opposite concept is *abstract administrative acts*, which cannot be reviewed by courts under the ALL. These acts are administrative acts with general binding force upon a group of unspecified people. Article 12 of the ALL exempts four categories of administrative acts from judicial review, one of which is *abstract administrative acts* such as regulations, rules, or other decisions formulated by administrative agencies and that have general binding force on unspecified groups of people.[425] The other three

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419 Articles 2 and 70 of the ALL.

420 Article 14 of the ALL.

421 Article 16 of the ALL.

422 Article 3 of the ALL.

423 'Opinion of the Supreme Court on the Implementation of the ALL', issued by the Supreme People's Court, in the *Bulletin of the Supreme People's Court*, No. 3, 1991.

424 Article 11 of the ALL.

425 Article 12 of the ALL.

categories excluded from judicial review are an administrative action involving national defense or foreign relations; decisions regarding rewards, punishments or appointments of administrative agency personnel, and decisions that are by law subject to the final jurisdiction of administrative authorities.[426]

### *Grounds for Judicial Review*

Article 5 of the ALL lays down the principle of legality as grounds for judicial review, meaning that 'When hearing an administrative case, a court shall inquire into the legality of a particular administrative action'. The ALL refers to illegality in five respects:[427]

- Lack of evidence;
- Violation of legal procedures. Under Article 54, a court shall annul or partially annul the administrative act if there is a 'violation of procedure'. However, the ALL does not provide for proper procedures, and there is no systemic Administrative Procedure Law in China. In practice, therefore, proper procedures can only be deduced from dispersed laws and requirements, such as specific procedural requirements in the relevant operative law, the general statutory procedural requirements and the independent non-statutory principles of fairness.[428] The concept of procedural fairness is still in its infancy in China,[429] and procedural requirements are frequently ignored when an administrative action in being adopted, especially in the case of normative documents adopted by sub-governmental administrative organs;
- Errors in the application of law. When adopting an administrative act, the administrative authority may apply a relevant law incorrectly or apply an irrelevant law. To judge whether an administrative action is based on accurate application of law is one of the most important steps in reviewing its legality since many problems arise in this area. There are two difficulties in seeking an accurate application of law. Firstly, as discussed in the chapter on transparency, Chinese legislation appears to be opaque and in disarray, with many conflicts between local rules and regulations. Courts have to choose which of the conflicting legal provisions to apply when deciding generally on the legality of an administration action or specifically when the administrative action is based on a rule which conflicts with other rules at the same hierarchical level. This task is particularly

426 Under the Patent Law of the PRC, adopted in 1992, decisions by the Patent Reconsideration Board under the Patent Bureau in respect of any request by an applicant, patentee, or the person who made the request for revocation for patent right, for reconsideration of a utility model or design was a final decision; see Article 43 of the Patent Law of the People's Republic of China 1992. However, the Patent Law was revised in 2000, and as the new version of the Patent Law abolished this provision, any decision by the Patent Reconsideration Board is now subject to judicial review; see Article 41 of the Patent Law of the People's Republic of China 2000.

427 Article 54(2) of the ALL.

428 David L. Weller, 'The Bureaucratic Heavy Hand in China: Legal Means for Foreign Investors to Challenge Agency Action', *Columbia Law Review*, June 1998.

429 David L. Weller,1998.

difficult for the court since its powers to review the legality of these conflicting rules is generally restricted, as discussed in more detail in the next part of this chapter. Secondly, the general or principle-based legal provisions that are common features of Chinese legislation leave wide discretion to the implementing authorities. This feature also increases the difficulty for the court when judging whether the administrative authority has properly understood and applied the relevant rules;

- *Ultra vires*. Courts are empowered to strike down an administrative act that is exercised in a way that exceeds the authority granted or is without authority;
- Abuse of authority. At least three essential elements need to be satisfied to differentiate between the abuse of authority and an exceeding of authority. For an abuse of authority, the authority exercised must be within the formal jurisdiction of the administrative organ; it must contradict or deviate from the objective and principle of the relevant legislation; and it must relate only to the exercise of discretionary power.

#### *Remedies*

If an administrative act falls into any of the above five categories, the court shall annul or partly annul the administrative act, or the administrative organ may be required to undertake a new administrative act.[430] If an administrative organ fails to perform or delays in performing the obligations imposed by law, the court shall set a fixed time for the administrative organ to perform the obligation.[431] If an administrative penalty is obviously unfair, it can be amended by the judgment.[432] Citizens, legal persons and other organization have the right to claim compensation for the damage caused by the infringement of their legal rights and interests.[433] The claim for compensation will firstly be dealt with by the administrative organ concerned.[434] Anyone refusing the disposition by the administrative organ may file a lawsuit in court.[435]

### 4.3.4 Practices under Current Legislation

China's judicial review is tantamount to 'administrative litigation'. The promulgation of the ALL has disseminated the concept that 'citizens can sue the government' (*min gao guan*). This stands in sharp contrast to traditional culture, with its old saying of 'better to be poor than a thief, better to have a grievance than to complain to government'.[436] The gradual increase in the numbers of administrative litigation cases suggests a rise in people's consciousness

430 Article 54 (2) of the ALL.
431 Article 54 (3) of the ALL.
432 Article 54 (4) of the ALL.
433 Article 67 of the ALL.
434 Article 67 of the ALL.
435 Article 67 of the ALL.
436 'Better to be poor than a thief, better to have a grievance than to complain to government' –*'qiongsi bu zuoze, yuansi bu gaozhuang.'*

of their rights. However, the caseload of administrative litigation cases in China is still very small.[437] Between 1990 and 2002, courts across the country accepted around 60 million first-instance criminal, administrative, civil and commercial cases, with administrative cases accounting for only slightly more than 1% of these.[438] Since approximately 75% of Chinese laws are administrative laws and regulations, administrative cases could be expected to account for a higher percentage.[439]

Another notable phenomenon is that the withdrawal rate of administrative litigation cases is very high. In other words, many administrative litigation cases are filed but later withdrawn by plaintiffs. This is one of the most intriguing puzzles in analyzing the effects of the ALL.[440] Between 1989 and 2008, the withdrawal rate was never lower than 30%, while the highest withdrawal rate, in 1997, was 57.3%. The reason for the high withdrawal rate and the way in which it undermines the effectiveness and integrity of China's administrative litigation system are discussed in detail in the following part of this chapter.

437 Veron Mei-Ying Hung, 'China's WTO Commitments on Independent Judicial Review: Impact on Legal and Political Reform', *American Journal of Comparative Law*, issue 52, 2004.

438 Veron Mei-Ying Hung, 2004.

439 Veron Mei-Ying Hung, 2004.

440 Pei, Minyin, 'Citizens v. Mandarins: Administrative Litigation in China', *The China Quarterly*, No. 152, December 1997.

**Table 7: Statistics of Administrative Litigation/Judicial Review Cases in China (1989-2008)**[441]

| Year | Number of cases accepted | Number of cases settled | Rate of withdrawal (%) | Rate of cases settled in favor of defendant (%) | Rate of cases settled in favor of plaintiff (%) | Rate of cases ended by other means (including cases rejected) (%) | Rate of cases rejected (%) |
|---|---|---|---|---|---|---|---|
| **1989** | 9934 | 9742 | **30.4** | 42.4 | 20.0 | 7.2 | |
| **1990** | 13006 | 12040 | **36.1** | 36.0 | 20.0 | 7.9 | |
| **1991** | 25667 | 25202 | **37.0** | 31.6 | 21.2 | 10.2 | |
| **1992** | 27125 | 27116 | **37.8** | 28.1 | 22.0 | 12.1 | |
| **1993** | 27911 | 27958 | **41.3** | 23.6 | 23.8 | 11.3 | |
| **1994** | 35083 | 34567 | **44.3** | 20.6 | 21.3 | 13.8 | |
| **1995** | 52596 | 51370 | **50.6** | 17.3 | 17.6 | 14.5 | |
| **1996** | 79966 | 79537 | **54.0** | 14.5 | 18.3 | 13.2 | *8.7* |
| **1997** | 90557 | 88542 | **57.3** | 12.7 | 16.8 | 13.2 | *8.5* |
| **1998** | 98463 | 98390 | **49.8** | 13.6 | 17.0 | 19.6 | *11.0* |
| **1999** | 97569 | 98759 | **45.0** | 14.9 | 18.2 | 21.9 | *12.0* |
| **2000** | 83533 | 84112 | **37.8** | 16.0 | 19.7 | 26.5 | *13.3* |
| **2001** | 98372 | 93219 | **33.3** | 17.1 | 17.9 | 31.7 | *14.7* |
| **2002** | 80728 | 84943 | **30.7** | 24.7 | 16.1 | 28.5 | *15.2* |
| **2003** | 87919 | 88050 | **31.6** | 27.8 | 14.3 | 26.3 | *10.7* |
| **2004** | 92613 | 92192 | **30.6** | 25.8 | 15.9 | 27.7 | *11.0* |
| **2005** | 96178 | 94771 | **30.2** | 16.6 | 17.4 | 35.8 | *11.4* |
| **2006** | 95617 | 94215 | **33.8** | 17.8 | 14.2 | 34.3 | *12.3* |
| **2007** | 101510 | 100683 | **37.0** | 29.1 | 12.6 | 21.2 | *9.1* |
| **2008** | 108398 | 109085 | **35.9** | 28.7 | 17.9 | 23.5 | *8.3* |

441 The data in this table are a combination of statistics provided by the Statistics Department of the Research Office under the Supreme People's Court, and the China Law Yearbook.

## 4.4 OBSTACLES TO JUDICIAL REVIEW IN CHINA

The effectiveness of the Chinese judiciary, with regard to its enforcement and independence, is highly unsatisfactory. This is widely recognized and is clearly evidenced in the annual reports presented by the Supreme People's Court to the NPC, and in the frequent and prominent coverage of the topic in the Chinese and English legal press.[442]

### 4.4.1 General Problems existing in the Judiciary – Lack of Independence

The lack of an independent judiciary in China is one of the major problems limiting the effectiveness of judicial review. Interference from administrative and Party authorities is very common. Political backing from the CCP is often deemed necessary for the enforcement of court judgments. The president of the Supreme People's Court frankly admitted this when he stated that 'We must closely rely on the leadership of Party committees in the work of enforcement. Enforcement concerns a wide range of issues and involves many areas and departments. If we rely on the courts only, there will be many difficulties and problems as well as restrictions. Courts at all levels must frequently and actively report their work to the Party committees, inform them of the problems encountered and seek their attention and support'.[443] The lack of judicial independence fundamentally jeopardizes the function of the judicial review as a check and balance of the administrative authorities.

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442 See, for example, the Work Report of the Supreme People's Court, delivered at the Third Plenary Session of the Ninth NPC on 10 March 2000, Gazette of the Supreme People's Court, p. 42. The ineffective judicial enforcement is normally referred to as "*zhining nan*" (difficulties in enforcement) in China and is fully recognized by the Supreme People's Court; The speech by Li Guoguang (Vice President of the SPC) on 8 October 1997, the speech by Xiao Yang (President of SPC) on 7 May 1998, and the speech by Li Guoguang (Vice President of the SPC), on 3 August 1998. Full texts of these speeches can be found in The Enforcement Work Office of the Supreme People's Court, *A Collection of Practical Documents on Compulsory Enforcement (Qiangzhi Zhixing Shiwu Huibian)*, Beijing: Publishing House of Law, 1999, pp. 103-107, 107-108 and 112-116 respectively; Jianfu Chen, 'Mission Impossible: Judicial Efforts to Enforce Civil Judgments and Rulings in China', in Chen Jianfu (ed.), *Implementation of Law in China*, Kluwer Law International, 2002. Donald Clarke has conducted one of the most comprehensive and representative survey and analysis of the problems in enforcement of civil judgment in China. Donald C. Clarke, 'Power and Politics in the Chinese Court System: The Enforcement of Civil Judgment', *Columbia Journal of Asian Law*, vol. 10, No. 1, 1996.

443 Speech by Ren Jianxin (then President of the Supreme People's Court) at the first national Court Enforcement Work Conference on 23 April 1996, in *A Collection of Practical Documents on Compulsory Execution* (Qiangzhi Zhixing Shiwu Huibian), The Execution Work Office of the Supreme People's Court , Beijing: Publishing House of Law, 1999.

#### *4.4.1.1 Governmental Organs, Status of the Party and Relationship to the People's Courts*

The Chinese Constitution sets out the basic state structure of China, under which the National People's Congress (NPC) is the highest power organ with supreme legislative authority, the State Council is the highest executive organ, and the Supreme People's Court the highest adjudicative organ. There are four levels of courts of general jurisdiction in China: the Supreme People's Court at the central level, the Higher People's Court at the provincial level, the Intermediate People's Court in prefectures and the Basic People's Court at the county or district level. Each court normally has one president and several vice presidents, judges/adjudicators (*shen pan yuan*), assistant adjudicators (*zhuli shen pan yuan*), administrative officials, judicial clerks and judicial policemen. The Constitution also states that the people's courts at the local level are responsible to the corresponding level of people's congress that creates them. The people's congresses have the power to appoint court personnel. Under the Organic Law on People's Courts and the Judges Law of China, the president is elected by the people's congress at the corresponding level. Vice presidents, judges and members of judicial committees are nominated by the president for appointment to or removal from the standing committee of the people's congress at the corresponding level.

However, the situation as described in books differs from the reality. Firstly, neither the Constitution, nor any other formal legal document, provides any definition or instruction on the leading role of the CCP and the Communist Party cadres. The CCP's importance lies in political reality and circumstance. The CCP keeps control over the state, mainly by exercising control over civil service appointments in two ways: the *nomenklatura* system and by demanding political loyalty as a requirement for jobs in the civil service.[444] All state organs, including courts, essentially have Communist Party organizations built into their structure. A court president, for example, is often also the head of the Communist Party Secretariat set within the court.. In addition to state organs, there is an established Party system (i.e. Party congress, Party committee and Party secretariat) at all local levels, supervising the work of the state organs and deciding on important appointments of state organs such as the government and the judiciary.

Secondly, the NPC does not in reality exercise the highest power in China, but instead serves as a 'rubber stamp' legislator for the State Council. Bills used to be passed unanimously. This has changed over the years, however, as the number of dissenting votes has gradually increased and the NPC has gained more independence as a legislator.[445] Although the NPC has moved away from its previous symbolic role and has become quite active as the forum in

444 For a detailed discussion of how the party controls the state, see Benjamin van Rooij, 'China's System of Public Administration', in Jianfu Chen, Yuwen Li and Jan Michiel Otto (eds.), *Implementation of Law in People's Republic of China*, Kluwer Law International, 2002, p. 323.

445 K. Lieberthal, *Governing China, From Revolution through Reform*, W.W. Norton & Company, New York, 1995, p. 162.

which legislation is debated before being put to a vote, it is still rare for the NPC to formally defeat a proposal put before it.[446] Ming Xia's recent study demonstrates that, at local levels, provincial people's congresses (PPC) play an explicit role in China's legislative system.[447] They do not merely 'rubber stamp' bills from the executive branch; they also initiate and sponsor many important bills.[448] However, this does not prove that the status of the PPCs vis-à-vis the executive or political authorities has changed, or that the PPCs have developed any power that can compete with executive or political authorities. Local people's congresses are actually still under the control of local governments and party organizations. There is, for instance, a specific body – the Political-Legal Committee (*zheng fa wei yuan hui*) – through which the Party supervises and coordinates with the people's court at the same level. The main task of the Central Political-Legal Committee is to set national legal policy, while the local Political-Legal Committee generally focuses on certain personnel, ideological and policy matters of local judicial organs, including the court, the Procuratorate and the public security force. Personnel matters mainly relate to the nomination of senior court officials, such as the president, vice president and division head. While personnel matters of the court are theoretically decided by the people's congress, nominations are usually discussed by the Political-Legal Committee before being forwarded to the people's congress at the corresponding level for confirmation.

Thirdly, since the real power is actually held by the party and often exercised by the administrative authorities, the 'administrative' branch (i.e. the State Council and local governments) effectively has significant control, including in the allocation of financial resources and personnel control, over the 'judicial' branch (i.e. courts and procuratorates at the same levels). Like the officials in administrative organs, court personnel have a bureaucratic rank, i.e. *keyuan*, *ke*, *chu*, *ting*, etc. Judges are treated as governmental administrative officials in the same way as officials in administrative organs.

The structural arrangements at state organs, as well as the unique status of the Party, account for the lack of independence of the people's court. The dominance of the administrative institutional model makes the court, to a certain degree, an instrument in the local authority's governance and breeds local protectionism in judicial practices.[449] Under this system, it is not surprising to see substantial interference from administrative authorities in judicial decisions, and to see the difficulty and reluctance the court experiences in reviewing administrative decisions.

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446 To date the full NPC has still rarely voted against a bill and remains a rubber stamp, albeit a more critical one; see 'China's National People's Congress: Democracy in Action – Making Sure that China's Supreme Legislative Body is Toothless', *The Economist*, 25 February 2010.

447 Ming Xia, *The People's Congresses and Governance in China – Toward a network mode of governance*, Routledge, 2008, p. 4.

448 Ming Xia, 2008, p. 4.

449 Chris X. Lin, 'A Quiet Revolution: An Overview of China's Judicial Reform', *Asian-Pacific Law & Policy Journal*, June 2003.

### *4.4 1.2 External Interference*

External interference as used here refers mainly to interference by the Party, local governments and administrative authorities. The excessive dependence of the courts – for their funding and for the appointment of judges – on political entities and local financial departments undermines the ability of the courts to impose meaningful restraints on external interference. It should be noted, however, that lack of independence does not mean that the Party and local governments control every action of the courts or determine the outcome of all or even most cases. In practice, the Party and administrative authorities intervene with the courts only in certain ways and through certain channels. The party organs and administrative authorities may exert influence in ideology, policy, personnel matters, and even in decisions in particular cases. Examples of party-led or -inspired policies include the various strikes and campaigns to reduce crime, the Guidance Notice regarding Lawyers' Handling of Multi-party Cases, prohibitions on accepting Falun Gong cases, and efforts to reduce judicial corruption.[450] Although they are not legally allowed to interfere, these organs or individual party members do on occasion become involved in deciding the outcome of particular cases.

External interference is particularly common in two specific circumstances. The first one is in the adjudication of 'major and complex cases', where external interference is permitted by law. 'Major and complex cases' can also be understood as politically sensitive cases or cases involving conflicts between courts and governments. In contrast to ordinary cases, the adjudication of 'major and complex cases' has to be made by a special adjudication committee consisting of the president and vice president of the court, as well chief judges from various divisions of the court.[451] The special committee usually makes the decision after consultation with the Political-Legal Committee at the corresponding level.[452] As indicated by the government document, one of the main responsibilities of the Political-Legal Committee is to 'supervise and discuss the adjudication and execution of major and complex cases, [and to] coordinate when contradictions arise among different judicial organs'.[453] This decision-making mechanism opens a door for administrative officials and Party members to intervene in judgments in particular cases.[454]

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450 Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, Cambridge University Press, 2010, p. 79.

451 Article 11, Organic Law of People's Court of China, revised on 31 October, 2006.

452 Meng Hou, 'Political-legal Administration in the context of Judicial Reform – Case Study on Local Political-Legal Committee', *Journal of East China University of Politics and Law*, issue 5, 2003; Hui Zhang, 'How the Political-Legal Committee Undermines the Rule of Law and Judicial Independency in China', *China Weekly (Gongmin Yibao)*, 19 September, 2010. http://www.chinaeweekly.com/new/FileView.aspx?FileIdq=969.

453 See, for example, the governmental document issued by Tulu Fan District, Xinjiang Province, stipulating the functions and components of governmental agencies, including the Political-Legal Committee of the District. http://www.tlf.gov.cn/1$001/1$001$003/1$001$003$002/97.jsp?articleid=2004-6-4-0045.

454 Mei Ying Gechlik, 'Judicial Reform in China: Lessons from Shanghai', Columbia Journal of Asian Law, Spring/Fall 2005.

The second one reflects how the party can flexibly use its policy to exert influence in adjudication. A judicial policy promoted by the government emphasizes 'dual goals' that need to be achieved in adjudication, i.e. 'unification of legal goals and social goals'. It is explained that 'to achieve the legal goals, adjudication has to strictly follow laws; to achieve social goals, adjudication has to satisfy specific needs of society and public'.[455] The former president of the Supreme People's Court, Xiao Yang, stated in his speech at Yale University in 2004 that:

> For a country approaching to rule of law, law shall be the chief element that needs to be considered for judicial organs and judges. Traditionally, however, China is a country developed from and deeply rooted in *'li'*/rites.[456] Law is impossible to become 'catholicon' for all disputes. Elements beyond law, such as morality or rules of propriety, cannot be ignored in judicial activities. Therefore, China's judicial organs advocate a judicial policy as to unify legal effects and social effects in adjudication.[457]

The emphasis on 'social effect' in this judicial policy, which was first introduced in 1999, was designed to meet the needs of a society transforming from a planned economy to a market economy. It is deemed difficult, in the transition process, to rely solely on legal provisions for adjudication because the legal system is unfledged and it often lags behind rapidly changing social conditions. The Party's policies, by contrast, are more flexible in reflecting the up-to-date needs of society. The pursuit of 'social effect' is of particular importance in eliminating social conflicts and promoting harmony under the current political slogan of 'establishing a harmonious society' referred to by President Hu Jintao.

Under this policy, courts are required to adopt a flexible and operable mechanism in adjudication in order to strike a balance between the rule of law and special needs of the society, specifically social stability and economic development. Examples that demonstrate the problem of achieving social goals at the expense of legal goals include politically sensitive cases (such as Falun Gong cases) and socio-economic cases (such as eviction cases). In eviction cases, social stability has been prioritized over adherence to law. Rapid urbanization means eviction lawsuits against governmental authorities have been common in China, especially in Shanghai, but the occasions on which governmental authorities have

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455 Bixin Jiang, 'Unification of Legal Effects and Social Effects', People's Daily, 10 May 2006.

456 *'Li'* (rites or rules of propriety), as a concept advocated in Confucianism, is a set of generally accepted social values and norms of behavior, and is rooted in innate human feelings. In contrast, 'fa' (human-made laws) is advocated by Legalism and refers to penalty for criminals. *'Li'* forbids trespasses before they are committed, whereas *'fa'* punishes criminal acts after they have been committed. Thus, law can supplement *li* by providing people with appropriate models via a mixture of rewards and penalties. *Li* and *fa* represent a conceptual dichotomy which is traditional in China. For more information, see http://en.wikipedia.org/wiki/Chinese_law.

457 Xiao Yang, 'China Judiciary: Challenges and Reform', published by People's Judiciary, 2005.

lost have been few.[458] Members of adjudication committees in the courts and local Political-Legal Committees are reluctant to rule against governmental authorities, fearing that such opposition would hinder urbanization and economic development.[459]

Being a general principle, the policy does not provide any precise explanation on how to achieve the goals, and judges thus face difficult choices if policy or social goals conflict with legal provisions. According to a director of a basic people's court in China, 'courts have to pursue the procedural and substantial justice according to laws on the one hand, and to safeguard and pave the way for economic development and society's stability on the other hand. Therefore, courts face extreme difficulties, like walking upon thin ice, when dealing with sensitive cases'.[460] He accordingly suggests that 'before the judiciary is capable of being completely immune of interference, courts have to learn how to establish a smooth relationship with all the supervisory organs, including administrative, legislative as well as the Party Committee. Otherwise, the dual goals cannot be unified. More specifically, it means that courts need to obey the leadership of the Party Committee, be subject to full supervision of People's Congress, and all the judiciary activities need to take the policies of the Party committee into consideration'.[461]

Despite the impact of the party organs, interference from local governments cannot be ignored. Local judicial protectionism, being rulings and judgments by judicial authorities who favor local parties and local economic interests but disregard facts as the basis and law as the criterion, has traditionally been common. The problem of such protectionism is so serious that it has been repeatedly reported by the Supreme People's Court to the annual conference of the National People's Congress.[462] As the Supreme People's Court discovered, it is not uncommon for local government organs to threaten to cut the court's funding or to remove judicial personnel from the court in order to compel courts to act according to various local 'internal documents' or policies.[463]

The absolute leadership of the Party and the policy guidance in adjudication give the Party organs, as well as local governmental authorities, ample opportunity to allow policy choices

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458 Mei Ying Gechlik, 2005.

459 Mei Ying Gechlik, 2005.

460 Sheqiu Li, director of the people's court of Shimen City, Hunan Province, 'Unification of Legal Effects and Social Effects in the Adjudication by People's Courts', published in China Courts Net, 31 January 2005, available at http://www.chinacourt.org.

461 Sheqiu Li, 2005, available at http://www.chinacourt.org.

462 It has been a constant theme at annual national judicial conferences since 1988. See, for example, Work Report of the Supreme People's Court, delivered at the First Plenary Session of the Eighth National People's Congress, 31 March 1993, Gazette of Supreme People's Court, p. 55.

463 Special Investigation Group, Supreme People's Court, 'Investigation Report on Local Protectionism in Judicial Activities', 18 July 1996, pp. 12-14, document in Chen Jianfu's personal file. See Jianfu Chen, 'Mission Impossible: Judicial Efforts to Enforce Civil Judgments and Rulings in China', in Jianfu Chen (ed.), *Implementation of Law in China*, Kluwer Law International, 2002, p. 99.

to prevail over the rule of law. Courts have to exercise great caution in dealing with sensitive cases and reconciling legal requirements with social effects. This demonstrates that the political and administrative authorities in China are still accustomed to using law as a tool, an instrument or a pragmatic device to effectuate their policies, although the legal reforms seen in the past 20 years have achieved gradual progress in enhancing the essential role of law, including protecting basic rights of citizens.

#### *4.4.1.3 Internal Interference – Court's Self-Restraint*

Despite the Party's absolute leadership and the external interference, courts have strategically pursued their own institutional interests and attempted to increase their status and authority. In order to gain more opportunities to develop and establish smooth relationships with all supervisory organs, the courts understand that they must take care not to challenge the regime on key issues that threaten the regime's authority to rule. One strategy they can adopt is to exercise self-restraint, as evident in certain types of corporate cases and even more clearly in high-profile cases involving political dissidents.[464]

Self-restraint may take many forms in practice. For instance, the court may sometimes refuse to accept cases for fear of insulting the Party and governmental officials, damaging relations with the local government or going against state policy. A concrete example is the Shanghai court's rejection of certain types of corporate cases between 1992 and 2008.[465] The survey found a large number of cases in which the court actually worked against the law in the service of a state policy aim. A case in 2006 is indicative of this value choice. In this case, shareholders of a limited liability company sought judicial dissolution. The application for dissolution was refused by the court because it was seen as a drastic and disruptive remedy, and it would alter the arrangements for paying salaries to laid-off workers. In a commentary, the Shanghai High Court lauded the court's refusal to approve the dissolution because of the negative impact this would have on market stability and the attendant social costs. Another illustrative example is the fact that very few cases relating to companies limited by shares (joint stock companies) were accepted by Shanghai courts between 1992 and 2008. One rationale behind the refusal is the fear of large plaintiff groups and the perceived threat to social stability or the impact on the 'super value' in Chinese administrative-political culture: social harmony.[466] The No. 2 Civil Division of the Shanghai High Court alluded to this

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464 Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, 2010, p. 15.

465 Survey conducted by Nicolas Calcina Howson, 'Judicial Independence and the Company Law in Shanghai Courts', in Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, 2010, pp. 134-153.

466 Nicolas Calcina Howson, 'Judicial Independence and the Company Law in Shanghai Courts', in Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, Cambridge University Press, 2010, p. 146.

apparent red line in its grudging reversal of a pre-2006 policy barring lawsuits that sought to invalidate public company resolutions:

> In view of the fact that these kinds of cases may give rise to issues related to mass litigation and volatility in the securities markets, [the Shanghai courts] have taken an especially cautious attitude towards accepting these cases; in accepting these cases, we ask that the shareholders provide related evidence showing why the shareholders or board resolution is invalid or should be invalidated, and we will examine this evidence strictly so as to protect against vexatious shareholder litigation.[467]

The above is evidence that the courts act as administrative units, prioritizing national social and economic policy over more specific mandates and rights set forth in company law. Another example of self-restraint is when a court tries to duck a case by suggesting to the plaintiff that he or she is not likely to win and should drop the suit.[468] It is most evident in judicial review cases, where the court is hesitant to confront the administrative masters. The consistently high withdrawal rate of judicial review cases is partially attributable to voluntary restraint by courts.

Institutional arrangements, more specifically the financial and personnel dependence of the court, are the major cause of the lack of judicial independence in China. It can be argued that external interference may not necessarily undermine judicial independence since some judicial policies and Party-involved judicial campaigns can help the court implement its rulings and judgments more effectively, and thus enhance judicial authority and effectiveness, which are indispensable elements of an independent judiciary.[469] This argument has some merit in that it reminds us a different angle from which to view the development of the judicial system in this developing and authoritarian country. As a developing country, China is experiencing a holistic reform process, involving interrelated changes in the social, economic, political and legal spheres. Given the lack of the resources needed to solve all the problems at once, the question of sequencing and prioritizing the reforms is one of the most difficult challenges facing China.[470] Sacrificing the value of the rule of law and judicial independence to the other values may in certain circumstances may be justified as the Party's choice for holistic reasons. In this authoritarian country, the Party is unchallengeable and the judicial system is underdeveloped. It cannot be denied that, in

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467 Shanghai High Court No. 2 Civil Division (ed.), "Judicial Investigation of Application of the New 'Company Law' in the Shanghai Courts after One Year" ("*Shanghai fayuan xin 'gongsifa' shishi yi zhounian sifa diaocha*"), *Company Law Review (Gongsi falu pinglun)*, 2007, p. 44.

468 Randall Peerenboom, 'Globalization, Path Dependency and the Limits of Law: Administrative Law Reform and Rule of Law in the People's Republic of China', *Berkeley Journal of International Law*, 2001.

469 Suli Zhu, 'The Party and the Courts', in Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, Cambridge University Press, 2010, pp. 52-68.

470 Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, 2010, p. 13.

some areas, the Party's intervention and government cooperation, mostly during judicial campaigns, can help the court enhance its efficiency and authority. However, it is important to realize that this political backing can lead to short-term gains only. Tolerating external interference carries with it the danger of reinforcing the conception of law as a tool for the ruling party. In the long term, this will result in a loss of respect for the law among the general populace, impair judicial authority, and hinder the development of the rule of law in China. More importantly, although the interference from the Party and government may not necessarily sacrifice justice in non-sensitive criminal, commercial or civil cases, it makes it much easier to undermine justice in judicial review cases where administrative authorities are challenged.

### 4.4.2 Specific Problems in Judicial Review

#### *4.4.2.1 Limited Scope of Judicial Review – Reviewability of Abstract Administrative Acts*

The scope of judicial review differs from country to country, as illustrated in Table 8. Normally, it includes a review of primary legislation (which is passed directly by legislature) and a review of administrative acts (including administrative decisions/resolutions and administrative decrees). Administrative decisions/resolutions are addressed to a particular person and contain a decision made by an administrative power or body that influences that person's patrimony rights or interests. Administrative decrees are legally enforceable rules of general applicability adopted by administrative bodies in order to fulfill public administration duties.

**Table 8: Comparison of Scope of Judicial Review in China and Western Countries**

| Countries | Judicial Review of Administrative Acts | | Judicial Review of Primary Legislation |
|---|---|---|---|
| | Administrative Decisions | Administrative Decrees | |
| United States | Reviewable by regular courts[471] | | Reviewable by regular courts |
| France/ Germany | Reviewable specially by administrative courts | | Non-reviewable by regular courts, but reviewable by constitutional courts |
| UK/ Netherlands | Reviewable by regular courts | | Non-reviewable by judicial organs (doctrine of Parliamentary Sovereignty) |
| China | Reviewable by regular courts | Non-reviewable by judicial organs | Non-reviewable by judicial organs |

471 'Regular courts' as mentioned in this table are the opposite of special courts such as administrative courts and constitutional courts.

Although Western countries have differing practices on the reviewability of primary legislation, they all allow courts to review two kinds of administrative acts. China, by comparison, is the only one that excludes administrative decrees, which it terms as 'abstract administrative acts', from the scope of judicial review.[472]

Excluding abstract administrative acts from judicial review creates enormous difficulties for reviewing concrete administrative decisions in China. The following example is illustrative. On 15 December 1998, Jiuquan (a city in Gansu province) Intermediate Court revoked an administrative punishment decision made by Jiuquan Technical Supervision Bureau.[473] The reason was that the provisions on administrative punishment provided in the 'Regulations on Quality Supervision of Gansu Province', on which the administrative punishment in question was based, were in conflict with the 'Administrative Punishment Law'.[474] The People's Congress of Gansu province decided, however, that the Jiuquan Intermediate Court's ruling infringed the legislative power of the local people's congress enshrined in the Constitution, and thus transcended its adjudication authority.[475] As a result, the High Court of Gansu Province, under the supervision of the People's Congress of the province, revoked the ruling of the Jiuquan Intermediate Court on 1 September 1999.[476]

If the court is not allowed to make judgment on the consistency of local regulations or rules, administrative decisions that are against central laws cannot be efficiently revoked or stopped. This rigid requirement undermines the effectiveness of the judicial review of administrative decisions and hinders the court from protecting individual rights that may be infringed by administrative organs. As an alternative, the Chinese legal system provides a law-reviewing mechanism conducted mainly by legislative and administrative bodies rather than judicial organs.

#### *4.4.2.1.1 Ineffective Legislative Review*

Under the Chinese Constitution, the consistency of laws is reviewed either by the legislature or by the administrative organs at the next higher level, depending on the categories of the laws. The NPC and the Standing Committee of the National People's Congress (SCNPC) are entitled to revise or annul laws, administrative regulations and local regulations that contravene the Constitution or superior laws.[477] The State Council has the authority to revise or annul inappropriate rules, decisions or orders issued by state departments at the

472 The ALL Article 12.

473 Jiejun Yang, 'China's WTO Accession and Reforms on Administrative Litigation', *Legal Science*, No. 4, 2002.

474 Jiejun Yang, 2002.

475 Jiejun Yang, 2002.

476 Jiejun Yang, 2002.

477 Article 67 (1), (2), (7) and (8), Constitution of the People's Republic of China. See also Article 88 (1) and (2), Legislative Law of the People's Republic of China.

central level or organs of state administration at local levels.[478] The local people's congress has the authority to revise or annul inappropriate local rules issued by local governments, while local governments can revise or annul inappropriate local rules issued by inferior local governments.[479] Table 9 provides more detailed clarification.

**Table 9: Law-Making and Law-Reviewing Authorities in China**

| Legislation | Law-Making Authority | Law-Reviewing Authority |
|---|---|---|
| Constitution | NPC | NPC |
| Law | NPC | NPC; SCNPC |
| Administrative Regulation<br>*Xingzheng fagui* | State Council | SCNPC |
| Local Regulation<br>*Difang fagui* | Provincial People's Congress and its Standing Committee | SCNPC;<br>Provincial People's Congress and its Standing Committee |
| Departmental Rule<br>*bumen guizhang* | Ministries, Commissions and Departments of State Council | State Council |
| Local Governmental Rule<br>*Difang zhengfu guizhang* | Local Governments | State Council;<br>Local People's Congress and its Standing Committee;<br>Local Governments at higher administrative level |

The many inconsistencies in Chinese legislation demonstrate that the existing review mechanism is not effective. This mechanism has preliminarily been created in a basic and unfledged legal framework and is far from an established, effectively functioning system. Firstly, the self-supervised review mechanism cannot ensure an impartial overview and check due to the problem in organizational structure. The above table shows that the SCNPC is the reviewing body responsible for the constitutionality and consistency of all Chinese laws, administrative regulations and local regulations. Given this heavy workload, however, it is surprising that there is no separate or specialized organ established under the SCNPC for such a review. In fact, as the beginning of 2006, the SCNPC had not revoked or invalidated a single regulation or law contravening the Constitution.[480] Secondly, there are no detailed and clear procedures for the reviewing process. The Legislation Law does not impose any

478 Article 88 (3), Legislative Law of the People's Republic of China.

479 Article 88 (5) and (6), Legislative Law of the People's Republic of China.

480 Linping Yang, Vice Director of Administrative Adjudication Chamber of the Supreme People's Court, *Several Problems of Judicial Review in China*, People's Court Publishing House, March, 2006, p. 41; Jinguang Hu, 'Four Flaws existing in Constitutionality Review in China', *Economy and Management Digest*, No. 3, 2006.

time limits on the whole process, and nor does it set any specific procedures, such as filing, review or decision-making procedures. In one instance, the State Council issued a written request, claiming that a local regulation was inconsistent with an administrative regulation.[481] It encountered great difficulties, however, before it could submit the request to the SCNPC because of the lack of detailed procedures in each step of the submission and in the reviewing process of the SCNPC.[482] Although the State Council finally submitted its request, the SCNPC has still failed to make a decision in the four years since the submission.[483] A long-awaited rule on how the NPC can achieve its supervision function, under which the reviewing of law is conducted, recently entered into force.[484] Unfortunately, this rule focuses only on how the NPC can supervise the implementation of laws (on a spot-check basis), but not on the consistency of laws.

The above defects mean that the existing law-review mechanism conducted by legislative organs has failed to effectively resolve the conflicts of laws. While people's congresses, which have the least opportunity to identify conflicts of law, have the most power of review in China, the courts that have most chance of discovering inconsistencies have the least power.

#### *4.4.2.1.2 Problem of Non-Reviewable Administrative Decrees*

As regards China's judicial review, the most disputable issue is the reviewability of administrative decrees issued by administrative organs at local levels. Most instances of inconsistency in China occur at the level of administrative rules, local rules and normative documents. The status of administrative decrees in judicial review needs further clarification since it is more complicated than it looks. While it is clear that the courts do not have the power to declare 'abstract administrative acts' invalid, it is unclear whether they are obliged to apply or disregard them where there is a consistency problem. According to Article 53 of the ALL, the courts can only apply laws and regulations when conducting judicial review. Rules, no matter whether they are administrative or local, can only be 'referred to' as opposed to 'applied'(*canzhao* as opposed to *yiju*) in judicial review cases. The meaning of 'referred to' has been interpreted to mean that if a rule does not conflict with superior laws,

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481 Wang Zhenmin, *Constitutional Review System in China*, China University of Political Science and Law Press, 2004, p. 135.

482 Wang Zhenmin, 2004, p. 135.

483 Wang Zhenmin, 2004, p. 135.

484 The rule is entitled the 'Supervision Law of the Standing Committees of People's Congress at all levels of the People's Republic of China, which was issued on 27 August 2006 and became effective on 1 July, 2007 Since being proposed at the 5th meeting of the Sixth National People's Congress in 1987, it has been under discussion at every meeting of the National People's Congress for nearly 20 years and was finally passed at the 4th meeting of the 10th National People's Congress in 2006. The NPC has three main functions: legislation, supervision and delegation. The review of the consistency of laws has been categorized as one of the major works under the NPC's supervision function.

then the court can refer to it in its deliberations. If, however, a conflict is found, the rule has no legal effect and the court can refuse to apply it. Unlike laws and regulations, which have to be applied by courts, the reference of rules is subject to the court's own selection. This selection needs a precondition, i.e. the court is authorized to investigate rules in order to determine whether they are consistent with superior laws and regulations. In this respect, the court therefore can conduct preliminary reviews on rules.

Apart from laws, regulations and rules, a considerable amount of normative documents is formulated by local governments and their functional departments in order to implement their administrative functions. Normative documents play an important role in bringing principle-like laws and regulations in China down to reality and local conditions through a process of specification.[485] They are issued by local governments at the county, town/village level. To a large extent, local functional departments also tend to base their acts on normative documents. However, neither the legal status nor the application of normative documents are provided for in the ALL or the Legislative Law.

The problem of the ambiguous status of normative documents, and the difficulty they add to the process of judicial review, has been widely recognized. Scholars have suggested that normative documents should be able to be referred to, at least where relevant laws or regulations do not exist. For the purpose of a more effective judicial review, the scholars suggested that normative documents should also be able to be referred to if they are necessary supplements to, but do not conflict with rules, regulations and laws.[486] In realizing the problematic status of normative document, the Supreme People's Court issued a note stating that:

> Although administrative agencies always refer to normative documents as their direct basis for the administrative actions, the normative documents cannot be considered as a formal legal source, and thus have no binding force on the courts. If the courts find the normative documents are legal, reasonable and appropriate, however, they shall recognize the effectiveness of those normative documents when judging the

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485 Peter Howard Corne, *Foreign Investment in China's Administrative Legal System*, Hong Kong University Press, 1997, p. 105.

486 See, for example, Quanxin Zheng and Li Yu, 'Study on Administrative Normative Documents other than Administrative Rules and Regulations – inspired by Wang Kaifeng Incident' (*Lun xingzheng fagui, guizhang yiwai de xingzheng guifanxing wenjian – you Wang Kaifeng Shijian yingqi de sikao*), *Administrative Law Review (Xingzheng Faxue Yanjiu)*, No. 2, 2003; Jie Li, 'An Analysis of Legal Status and Force of Normative Documents in Judicial Review' (Qita guifanxing wenjian zai sifa shencha zhongde diwei ji xiaoli tanxi), *Administrative Law Review (Xingzheng Faxue Yanjiu)*, No. 4, 2004; Lifang Chen, 'Analysis of Legal Status of Normative Documents' (*Xingzheng guifanxing wenjian de falv diwei fenxi*), *Party & Government Forum (Dangzheng Luntan),* No. 4, 2007; 'Legal Effect and Applicability of Normative Documents' (*Lun xingzheng guifan wenjian xiaoli yu shiyong*), *Journal of Tianjin University (Social Science)(Tianjin Daxue Xuebao-shehui kexue ban)*, No. 2, 2008.

> legality of administrative actions. The courts can explain whether the normative documents are effective in their final decision as one of the grounds for judgment.[487]

This note denies the formal legal status of normative documents; however, it allows courts to review the legality and consistency of normative documents. It also states that:

> When review[ing] the legality of an administrative action, the court shall at the same time make a decision on whether the inferior law (as the legal basis for an administrative action) conflicts with its superior law. If the court finds that the inferior law conflicts with the superior law, the court shall rely on the superior law to judge the legality of the questioned administrative action.[488]

The note suggests how courts should deal with inconsistency of laws in judicial review cases: in other words, bypassing the problematic law and applying the superior law directly. As discussed above, courts may have preliminary review power on 'rules'. The Supreme People's Court's suggestion shows that courts may also have certain preliminary review powers on the legality of all laws, regulations and rules. The limitation is that they do not have the power to declare the reviewed ones invalid.

Unfortunately, the effect of this note is unclear. Even if the note could become a rule with general binding force and be enforced by courts at all levels, there would still be two fundamental problems standing in the way of an effective judicial review. Firstly, although courts can decide to refrain from applying an administrative decree for reasons of inconsistency, the infringing decree may retain its validity and continue to be enforced, and thus any infringing administrative decisions based on this decree cannot be corrected. Secondly, the solution whereby courts ignore the problematic law and apply the higher law would not work in the way suggested. In practice, many detailed and implementing provisions are provided, and only provided, in rules or normative documents. Courts may not be able to apply the higher law for the simple reason that there is no specific provision, but instead only the general principles provided in the higher law.

The limited scope of judicial review, coupled with the ineffectiveness of the legislative self-reviewing system, means that inconsistent rules and normative documents will extensively continue to exist, and that infringing administrative acts will not be efficiently corrected. It acts as an obstacle preventing the court from protecting individual rights against administrative

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487 'Important Note of the Meeting on the Legal Application in the Adjudication of Administrative Litigation Cases', issued by the Supreme People's Court, May 2004.

488 'Important Note of the Meeting on the Legal Application in the Adjudication of Administrative Litigation Cases', issued by the Supreme People's Court, May 2004. This note was issued to and is required to be implemented by all the high courts of every province and autonomous region.

authorities, and thus exacerbates the systemic problem that the non-independent judiciary creates for judicial review in China.

#### *4.4.2.2 Case Study*[489]

In September 2004, Chengtian Automobile Trading Company (Chengtian Importer/plaintiff) in Hainan Province brought litigation in the Intermediate People's Court in Haikou city against the Commerce Department of Hainan province (Commerce Department/defendant) and its subordinated Office of Machinery & Electronic Products (M&E Office/defendant). The plaintiff claimed that the substantial application fees charged by the defendants for import licenses was illegal and thus requested a refund. In order to apply for the quota of automobile import licenses, the plaintiff, as required by the defendants, paid a total of 5,550,000 yuan (roughly EUR 550,000) between September 2002 and April 2004.[490] However, the defendants never issued any legal receipt to the plaintiff for the fees. The plaintiff decided to sue the defendants for the licensing fees charged, which it believed to be illegal and to damage its rights and interests.

Between 2002 and 2004, imports of automobiles in China were restricted by the quota-attached import licensing system. Automobile importers had to apply for quota-attached import licenses from the competent administrative authorities.[491] The rules regulating the administration and procedures for issuing quota licenses did not, however, include any provision on application fees.[492] In 2003, the importers reported the problem to the Ministry

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489 The source of the case: 'Administrative Ruling of the High Court of Hainan Province', Case Number: [2005] Qiongxing Zhongzi No. 53, 23 May 2005.

490 According to s claimed by the plaintiff, the application fees rose dramatically in September 2002 after an oral notice from the M&E Office. Based on According to the rates applying in of the second half of 2003, the fees for normal cars was RMB 70,000 yuan, while the fee for cross-country cars was RMB 50,000, yuan and for vans was RMB 30,000 yuan.

491 At the central level, the Ministry of Commerce and its National Office of Machinery & Electronic Products Office were in charge of the administering ration of import licenses. These authorities could allocate certain amounts of quota to each very province, and the provincial authorities could decide which qualified importers that were eligible for these quota licenses. If the applications were less than the quota, they could give ensure every importer a quota license. If the applications exceeded the quota, they would select which importers to issue the quota licenses to, based on the criteria set in the relevant laws and regulations. The criteria included the applicant's previous performance of the applicant in imports; whether the quotas in previous the past years had been fully used; the productive capacity, management of scale and sales of the applicant; the quantity of quotas applied for and so on; etc. See Article 16 of the Regulations on Administration of Import and Export of Goods, 1 January, 2002. The other relevant laws include the Foreign Trade Law 1994 (Article 20) and the Implementation Rules on Administration of Quotas for Machinery and Electronic Products 2001 (Articles 6 and 9).

492 Only a general provision in the Foreign Trade Law could be found; this stipulated that the import quotas should be allocated in line with the import performance and capacities of the applicants and on the basis of fairness, efficiency, openness and fair competition. See Article 20 of the Foreign Trade Law 1994, as well as the Foreign Trade Law 2004.

of Commerce in Beijing. After the investigation, the Ministry of Commerce identified the inappropriate practice of Hainan province and thus temporarily withdrew the quota licenses allocated to Hainan. In November of the same year, however, it reallocated the quota licenses to Hainan. After failing to obtain meaningful help from the superior administrative authority, the plaintiff (including the other fourteen importers) began paying the defendants substantial amounts of application fees. In order to circumvent the law that prohibits the sale of import licenses,[493] the defendants referred to the collection of application fees as 'fund-raising for foreign trade development'. They requested the importers to transfer a certain amount of money to this fund before the issuance of the import licenses. To further justify the fees, the Commerce and Finance Departments of Hainan province jointly issued a normative document entitled 'Preliminary Measures on the Administration of the Fund of Foreign Trade Development of Hainan Province'.[494] This document stated that income from bids or compensable uses of import or export quota licenses was one of the fund's three legal sources of revenue.

In the trial of the first instance, the intermediate court ruled against the plaintiff on the grounds that the litigation was beyond the scope of review under the ALL. The court held that, firstly, the license fees were voluntarily paid by the plaintiff, but not compulsorily charged by the defendants; charging the license fees was thus not a unilateral administrative action, but a bilateral administrative action. For this reason, it could not be regarded as an administrative decision reviewable under the ALL.[495] Secondly, the court ruled that the plaintiff could not prove how its lawful rights were being infringed by the defendants. By paying the license fees, the court stated, the plaintiff obtained a limited number of quota licenses from the defendants. The defendants' action was in fact, therefore, beneficial rather than detrimental to the plaintiff. Thirdly, the court ruled that whether the 'Foreign Trade Development Fund' and the related normative document were legal was also not subject

493 The Regulation on Import Licensing of Goods prohibits the purchase, sale, transfer, alteration and forging of import licenses. See Article 8, Regulation on Import Licensing of Goods 2001. Although the 2001 version has been replaced by the version of December 2004, Article 8 of the 2004 version contains the same provision.

494 This document was issued in August 2003, and the document number is Qiong Shangwufa [2003] No. 82.

495 In fact, the relevant laws do not make a distinction between unilateral and bilateral administrative acts and do not preclude the latter from the scope of judicial review. The relevant legal documents include the ALL and the Supreme People's Court's Interpretation on the Implementation of the ALL issued in 2000. Neither of these documents mentions or precludes bilateral administrative acts from the scope of review. A distinction between bilateral and unilateral administrative acts appeared once in the Opinion of the Supreme People's Court on the Implementation of the ALL (Trial Version) issued in 1991. However, it was replaced by the Supreme People's Court's Interpretation on the Implementation of the ALL issued in 2000. It should also be noted that although the Supreme People's Court's Interpretation issued in 2000 precludes non-compulsory administrative guidance from judicial review, it is not applicable in this case because the licensing fee was compulsorily charged in the sense that it was a necessary precondition for obtaining import licenses. Thus, the application fee charged is fundamentally different from non-compulsory administrative guidance.

to the scope of judicial review. Therefore, it rejected all the requests from the plaintiff. The plaintiff appealed to the High Court of Hainan Province. However, the High Court rejected the appeal and upheld the judgment of the first instance court.

The implication of this case is discussed below. Firstly, a restricted scope of review hinders the court in providing an effective review of administrative decisions addressed to a particular person. In the absence of a meticulous judicial review of the legality of normative documents in this case, or administrative decrees in general, the exercise of administrative power at a local level is not subject to any examination or restriction. As demonstrated above, the court could not rule on the concrete administrative decision without reviewing the legality of the normative document. The ALL does not, however, allow the court to make a formal and binding review of abstract administrative acts; nor does it prohibit the court from conducting an incidental review of abstract administrative acts, such as local rules and normative documents, at a lower level. Without a formal and explicit legal provision, it is wholly up to the court to decide whether to conduct an indirect or preliminary review of abstract administrative acts. The danger in the discretion available to the court is that the extent to which the court will exercise its judicial review power is unpredictable and inconsistent. This blurs citizens' expectations of and confidence in judicial review. In the context of a non-independent judiciary and local protectionism, the court may well opt to evade the issue, as happened in this case.

Secondly, the 'skip the problematic lower law but apply the higher law instead' solution will not always be feasible in practice.[496] In this case, the High Court skipped the normative document, but applied the departmental rule issued by the Ministry. However, the provision in the higher law failed to address the key question of whether setting high application fees constituted a *de facto* 'sale' of import licenses or whether it should be regarded as 'bidding', which was allowed by the higher law. The court can only implement the 'spirit' of the higher law in accordance with its own understanding. By comparison, local rules and normative document are much more indicative than higher laws of the real regulatory practices of administrative authorities. This is also part of China's legal reality – principle-like national laws have to be implemented and localized by local rules. In many cases, therefore, applying only the 'spirit' of higher laws will not resolve specific disputes.

Thirdly, the case also reveals the delicate relations between courts and governments, laws and policies. There are many obvious flaws in the court's ruling. For example, the 'beneficial rather than detrimental' argument of the first instance court is strikingly implausible and

496 'Superior law takes precedence over inferior law, special law takes precedence over general law' is a basic principle of law application in China. As mentioned above, the SPC's Note on Legal Application in the Adjudication of Administrative Litigation Cases also suggests that the court should apply directly to higher law if it finds there to be a conflict between lower law (legal basis of an administrative decision) and higher law. See footnote 487.

farfetched. It is readily apparent that the plaintiff may benefit from the issuance of the licenses, but will definitely not benefit from the substantial amounts of license fees paid. This judgment could be used to justify any discriminative and illegal charges or licensing fees imposed by administrative authorities. Moreover, the court was reticent on why the defendants had never issued any receipt for the license fees if, as ruled by the court, it was legal to charge for them. The court's ruling is clearly not solidly founded. Although there is no direct evidence of government intervention, such an absurd ruling seriously questions both the professional quality of the judge and the relationship between the government and the court, which seems to have acted as a defender of the government.

Lastly, with regard to the WTO requirements for import licensing procedures, non-automatic import licenses should not be trade restrictive or distortive on imports additional to those caused by the imposition of the restriction.[497] Non-automatic import licensing procedures should be no more administratively burdensome than absolutely necessary to administer the measure.[498] The substantial license fees charged by the defendants will obviously cause additional burdens for and restrictions on importers to an extent greater than is needed for administration purposes. They make the costs of imported automobiles much higher, and thus much less competitive, than domestic automobiles.

#### *4.4.2.3 Mediation in Judicial Review? – Trends in Future Judicial Reform*

Whereas mediation is encouraged in China's civil litigation, it is explicitly prohibited in administrative litigation[499] on the grounds that there is a great disparity between the plaintiff and defendant in administrative litigation, and administrative organs or officials may intimidate plaintiffs into settlement during mediation. For the same reason, the ALL also requires the court to carefully review applications by plaintiffs for cases to be withdrawn in order to prevent involuntary or forced withdrawal under pressure from administrative authorities.[500]

497 Article 3(2), Agreement on Import Licensing Procedures.
498 Article 3(2), Agreement on Import Licensing Procedures.
499 Article 50, ALL.
500 Article 51, ALL.

In reality, however, the court rarely reviews plaintiffs' applications for withdrawal;[501] this results in the intriguing puzzle in China's judicial review that large numbers of cases are withdrawn by plaintiffs.[502] Courts conduct *de facto* mediation between plaintiffs and defendants in many cases. They often persuade plaintiffs to drop cases by promising to discuss a concession with the defendant, by informing a plaintiff that the case is doomed to fail, or by offering to waive all litigation fees.[503] This *de facto* mediation has been referred to as 'coordination' (*xietiao chuli*) within the court system.[504] For both administrative organs and courts, 'voluntary' withdrawal by the plaintiff is probably the best result of an administrative litigation. In some places in China, 'losing an administrative litigation suit' is even counted as a negative factor when evaluating the performance of administrative organs.[505] The prohibition of mediation and the strict requirements on case withdrawal are designed for a more impartial judicial procedure that seeks to protect individuals' rights against administrative authorities. Quite often, however, Chinese courts opt to avoid confrontation with administrative authorities by means of 'coordination' designed to persuade the plaintiff to drop the litigation.

501 Many studies in China have analyzed the high withdrawal rate of administrative litigation cases and stated that one of the reasons for the problem is that the court has not fulfilled its task of reviewing the plaintiff's withdrawal. See Sun Linsheng and Xing Shuyan, 'Why the Withdrawal Rate of Administrative Litigation remains High? Investigation of 365 Administrative Litigation Cases', *Administrative Law Review (Xingzheng Faxue Yanjiu)*, No. 3, 1996; Xie Jianzhen, 'Problems and Countermeasures in the Withdrawal of Administrative Litigation Cases', *Law and Economics (Fazhi he Jingji)*, No. 5 1996; Li Hailiang and Luo Wenlan, 'Legal Reasons for Abnormal Withdrawal in Administrative Litigation', *Administrative Law Review (Xingzheng Faxue Yanjiu)*, No. 4, 1997; Zhao Zhengqun, 'Development and Challenges of Administrative Litigation Right and its Theory in China', *Procedural Law Review (Susongfa Luncong)*, vol. 6, 2001.

502 Table 7.

503 He Haibo, 'Investigation on the Withdrawal of Administrative Litigation from 1987-2008', in He Haibo (ed.), *Substantive Rule of Law – Seeking for Legitimacy of Administrative Adjudication*, Law Press China, 2009.

504 For a detailed study on 'coordination' in judicial review, see Zhou Gongfa, 'Comprising System in Administrative Litigation', *Administrative Law Review*, No. 4, 2005.

505 He Haibo, 2009.

Covert 'coordination' seems to be justified by several policies that have been issued by the central authorities since 2006.[506] These policies require local courts, wherever possible, to resolve administrative litigation through 'coordination',[507] especially in respect of collective litigation relating to rural land acquisitions, urban housing evictions, restructuring of state-owned enterprises, labor and social insurance and environmental protection.[508] Under the slogan of 'harmonious society', the Supreme People's Court issued a specific document to encourage 'coordination' as a new resort for administrative litigation and to require local courts to try their best to reconcile disputes between plaintiffs and defendants before making judgment.[509] The document states that, for the detailed procedures of 'coordination', courts can make reference to those mediation procedures provided for in civil litigations, and that a variety of resolving methods that can contribute to building a harmonious society should be encouraged.[510] In order to institutionalize the above judicial policies into formal rules, the Supreme People's Court promulgated a judicial interpretation in 2008 entitled the 'Supreme People's Court's Provision on Several Issues of the Withdrawal of Administrative

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506 On 4 September 2006, the State Council and the General Committee of the Communist Party of China jointly issued 'Opinions on Preventing and Settling of Administrative Disputes and Improving of Administrative Litigation System'(*Guanyu Yufang he Huajie Xingzheng Zhengyi, Jianquan Xingzheng Zhengyi Jiejue Jizhi de Yijian*), *Zhongbanfa* [2006] No. 27. This document seems never to have been published, but its main content and spirit can be inferred from several local government documents that are intended to implement this central policy. This document states that administrative disputes can be settled by multi-channels, including legislative, judicial and administrative methods. It emphasizes that the most important channel shall be administrative reconsideration, which shall be conducted by administrative authorities rather than judicial organs. It determines the 'three settlements' policy (*sanhuajie*) as the basic requirement in resolving administrative disputes, i.e. resolving disputes at grassroots level, resolving disputes at an early stage, and resolving disputes in administrative process. It emphasizes the importance of 'coordination' and 'mediation' in the 'three settlement' policy. See 'Opinions on Improving Administrative Litigation System – CCP Committee of Hainan Province and Hainan Province Government', issued on 22 December 2006, *Qiongbanfa* [2006] No. 42; 'Exploring Ways to Actively Resolving Administrative Disputes', Legislative Affairs Office of Ganzhou City Jiangxi Province, 8 April 2008, http://www.jxfazhi.gov.cn/2010-4/2010414112133.htm; Jia Guoxian, 'Introduction of China's Pilot Reform on Administrative Reconsideration Committee' (*Woguo Xingzheng Fuyi Weiyuanhui shidian gaige qingkuang jiejie*), *Xiamen Legislative Issues (Xiamen Fazhi)*, December 2010. http://www.chinalaw.gov.cn/article/xzfy/llyj/201101/20110100333105.shtml. In 2007, the Supreme People's Court also issued several official documents on this topic.

507 'Supreme People's Court's Opinions on the Improvement of Adjudication of Administrative Litigation' (Zuigao Fayuan Guanyu Jiaqiang he Gaijing Xingzheng Shenpan Gongzuo de Yijian), 24 April 2007, F*afa* [2007] No. 19.

508 'Supreme People's Court's Opinions on Enhancing the Role of Mediation in Building Socialist Harmonious Society' (*Zuigao Fayuan Guanyu Jingyibu Fahui Susong Tiaojie zai Goujian Shehuizhuyi Hexie Shehuizhong Jiji Zuoyong de Ruogan Yijian*), 1 March 2007, *Fafa* [2007] No. 9.

509 'Supreme People's Court's Opinion on Enhancing the Role of Mediation in Building Socialist Harmonious Society' (*Zuigao Fayuan Guanyu Jingyibu Fahui Susong Tiaojie zai Goujian Shehuizhuyi Hexie Shehuizhong Jiji Zuoyong de Ruogan Yijian*), 1 March 2007, *Fafa* [2007] No. 9.

510 Article 6, 'Supreme People's Court's Opinion on Enhancing the Role of Mediation in Building Socialist Harmonious Society' (*Zuigao Fayuan Guanyu Jingyibu Fahui Susong Tiaojie zai Goujian Shehuizhuyi Hexie Shehuizhong Jiji Zuoyong de Ruogan Yijian*), 1 March 2007, *Fafa* [2007] No. 9.

Litigation'.[511] This Provision states that if the court finds the specific administrative act to be illegal or improper, it can advise the defendant to change the act before making judgment.[512] In practice, the 'advice before judgment' provision allows the court to conduct mediation between the defendant and the plaintiff. It gives rise to an explicit conflict with the ALL, which prohibits mediation in judicial review. Tolerating this conflict suggests that compliance with central policies takes priority over compliance with law in judicial works.

The legalization of mediation demonstrates that satisfying special needs of Party policies can be placed above the pursuit of rule of law. Likewise, the 'Three Supremes' doctrine articulated by President Hu Jintao in 2007 requires judicial workers always to regard as supreme the Party's cause, people's interests, and the Constitution and laws in judicial works, in which the Party's cause is put in the first place.[513] There has in fact been considerable debate in recent years on the proper role of the judiciary in China, especially since 2008 when Wang Shengjun was appointed to replace Xiao Yang as head of the Supreme People's Court.[514] Many commentators have interpreted this as a conservative appointment likely to lead to more Party control of the judiciary and to more restraints on judicial independence.[515] Although the Politburo has reconfirmed its commitment to the rule of law and Hu Jintao emphasized in a major speech to mark the thirtieth anniversary of opening and reforms that the only way forward was to deepen reforms, several changed central policies, including the legalization of mediation in judicial review, reflect these seemingly inconsistent trends, i.e.

511 'Supreme People's Court's Provision on Several Issues of the Withdrawal of Administrative Litigation' was promulgated by the Supreme People's Court on 14 January 2008 and became effective on 1 February 2008, *Fashi* (Legal Interpretation) [2008], No. 2.

512 Article 1, 'Supreme People's Court's Provision on Several Issues of the Withdrawal of Administrative Litigation'.

513 Like all the other CCP doctrines, this doctrine is proving to be profoundly important in judicial works. It was first articulated by President Hu Jintao at the National Conference of Political-Legal Works, convened by the Party's Central Political-Legal Committee, on 26 December 2007. Since 2008, the new SPC president, Wang Shengjun, has been conducting a campaign within the court system to promote the doctrine of 'Three Supremes' (*sange zhishang*). See also Jerome A. Cohen, 'Body Blow for the Judiciary', South China Morning (Online), 18 October 2008.

514 Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, Cambridge University Press, 2010, p. 18.

515 Critics have noted that, in comparison to the more extensive legal and academically qualified background of Xiao Yang, Wang's background is much more that of a 'political-legal cadre'. It has been commented that the ascendance of Wang Shengjun to the position was not an encouraging sign for legal reformers. Wang rose to his new position through the public security and political affairs apparatus and appears to have been appointed not for his law credentials, but because he is a 'trusted party functionary'. At a national meeting of judicial and security officials in June 2008, Wang emphasized the necessity for the courts to uphold the 'three supremes' doctrine articulated by President Hu Jintao – the Party's cause, the people's interest, and the Constitution and laws. See the US Congressional-Executive Commission on China's 2008 Annual Report, 31 October 2008; Willy Lam, 'The CCP Strengthen Control over the Judiciary', China Brief (Online), 3 July 2008; Jerome A. Cohen, 'Body Blow for the Judiciary', South China Morning (Online), 18 October 2008; China's Human Rights Lawyers: Current Challenges and Prospects, CECC Round-table, 10 July 2009, Testimony of Professor James V. Feinerman, Georgetown University Law Center.

China's future judicial reform is moving towards a more moderate and conservative path. Wang has emphasized that 'The courts, law, and legal system are a means to economic growth, and thus judges need to consider the consequences for development when deciding cases'.[516] He has also emphasized the important role of the court in promoting social harmony.[517] In other words, adherence to the rule of law may need to be sacrificed for the pursuit of social harmony and economic development; if, for instance, strictly enforcing labor rights would push companies out of business, or protecting the environment would slow down economic development.[518] Once again, it proves that the question of how to sequence various developmental needs, which is the most important issue for a developing country such as China, remains a completely political decision. The most difficult challenge confronting the courts is what the role of the courts will be vis-à-vis Party organs, the Political-Legal Committee and local governmental authorities. This challenge is especially prominent with regard to judicial review. From one perspective, the trend can be viewed as a political compromise of the judiciary, while, from another perspective, this compromise may bring feasible reforms acceptable to other players and yet also make the judiciary more effective in responding to increasing demands and changing circumstances.[519] Nonetheless, the emphasis of the court's role in policy implementation hinders it from promoting the rule of law and reinforces instrumentalism of the 'rule by law' system.

## 4.5 EFFORTS TO IMPROVE JUDICIAL REVIEW IN FOREIGN TRADE REGIME

The key requirement of the WTO judicial review clause lies in the independent nature of the reviewing body and its ability to ensure an objective and impartial review. The main purpose of this requirement is to ensure uniform implementation of the WTO law and to provide a direct remedy at domestic level for individual trade actors as regards improper administrative decisions. Whether or to what extent China complies with the judicial review requirement are questions that the WTO adjudicative bodies have to answer on a case-by-case basis. The WTO treaty does not contain any general provisions on standards of review applying across the entire range of WTO disputes; nor do any individual WTO agreements contain such provisions applicable to all disputes.[520] Since China has not yet received any complaints on judicial review, it is difficult to judge the precise extent of its WTO compatibility.

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516 Wang Shengjun, 'Thoroughly Implement the Spirit of the 17th Party Congress – Resolutely Carry Out Each of the Court's Task' (*Shenru guanche luoshi dangde shiqi da jingshen – zhashi zuohao renmin fayuan gexiang gongzuo*), *Qiushi*, vol. 485, August 2008, p. 16.

517 Wang Shengjun, August 2008, p. 16.

518 Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, 2010, p. 19.

519 Randall Peerenboom (ed.), *Judicial Independence in China – Lessons from Global Rule of Law Promotion*, 2010, p. 20.

520 Sharif Bhuiyan, 2007, p. 145

From a macro point of view, this chapter demonstrates that the lack of independence of judicial review in China's domestic legal system hinders it to provide an effective and objective remedy for individuals. There are incredible impediments for the country to overcome if it is to comply with the WTO requirement. Despite the fact that China has committed to ensuring the tribunals responsible for review will be impartial and independent of the agency responsible for administrative enforcement, its legal reality points to the opposite. Moreover, the limited scope of China's judicial review is incompliant with the GATT rule which requires all laws, regulations, judicial decision and administrative rulings of general application to be subject to review. This limited scope undermines the court's function in enhancing uniform implementation of national laws, as well as WTO law incorporated in national laws. Like other systemic requirements, the impact of non-compliance with the judicial review requirement is not limited to the requirement itself. If improper administrative actions cannot be promptly corrected, foreign traders' rights and interests under many substantive WTO rules will be undermined. As demonstrated in the case studies, for example, unreasonable tariffs may be charged and continued to be charged on importers if WTO-inconsistent customs valuations cannot be corrected in the judicial review[521], or imported products may become less competitive than domestic products if the disguised illegal charge that the government imposes on imported products cannot be annulled by the court.[522]

Despite obstacles existing in domestic institutions, China has made some efforts to improve judicial review, specifically in the area of foreign trade, in order to bring it more in line with the WTO standards. Indeed, providing special or supra-national treatment for foreign businesses, with the aim of attracting foreign capital and investment during China's open door reform, is a common practice.[523]

### 4.5.1 Judicial Review for Foreign Trade-Related Administrative Actions

In 2002, the Supreme People's Court issued the 'Rule of the Supreme People's Court on Certain Issues Related to Hearing of International Trade Administrative Cases' (Rule of

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521 See the case study (*Zhaoqing Foreign Trade Company vs. Zhaoqing City Customs*) on customs valuation discussed in the following part.

522 See the case study (*Chengtiao Importer vs. Commerce Department of Hainan Province*) on application fees for import licenses discussed in Part II.

523 Since 1980s, foreign-invested enterprises in China have received many forms of preferential treatment, mainly related to tax policies and land use. For example, while the income tax for Chinese domestic enterprises was 30%, it was 15% for foreign invested enterprises. In 2008, a new law on income tax for all enterprises in China (Enterprise Income Tax Law of the People's Republic of China, implemented on 1 January 2008) revised the preferential treatments of foreign invested enterprises and reduced the gap between the treatment of domestic and foreign enterprises. It formulated a plan to gradually unify the treatment of domestic and foreign enterprises in China.

International Trade Administrative Cases).[524] This rule was enacted and construed for the purpose of ensuring fair and timely hearing of international trade administrative cases, on the basis of the ALL, the Legislative Law and other relevant laws. Article 1 manifestly accords with the WTO requirements. It defines international trade administrative cases as including administrative cases relating to trade in goods, trade in services, and trade in intellectual property rights. It also provides that where there are two or more reasonable interpretations of a provision of the applicable law or regulations available to the adjudication of international administrative cases, the court shall apply the one consistent with the corresponding provision of the relevant international treaty.[525] Foreigners and foreign organizations shall be entitled to the same standing as that of citizens and organizations of China.

The most notable change brought about by this rule is that it raises the level of the jurisdictional court of the first instance in judicial review cases in the area of foreign trade. Under the rule, the jurisdiction of the court of the first instance in international trade-related judicial review cases is subject to the intermediate or upper-level people's court, which contrasts with the situation applying in respect of the basic people's court provided for in the ALL.[526] The Supreme People's Court states that judges in courts higher in the hierarchy are more experienced, knowledgeable and competent, which will contribute to a better judicial review in foreign trade-related actions. More importantly, the courts with higher hierarchy have broader geographic jurisdiction and are accordingly less susceptible to local authorities. In theory, therefore, this should reduce the effects of local protection and local authority interference on judicial review.

Judicial review of foreign trade-related cases will be conducted under the framework of the ALL, which means abstract administrative actions are still not reviewable. Given the concerns about the problem of conflicts of law and inconsistent local rules, it has been emphasized that national laws and administrative regulations promulgated by the State Council will be used as the main legal basis for the judicial review of foreign trade-related cases, and local rules can be referred to only if they are consistent with national laws and are adopted within the authority of local legislative organs.[527] In practice, this specific rule has rarely been applied. It is probably the most feasible and low-cost option for the central government in order to make judicial review of foreign trade-related administrative decisions look more compatible with the WTO requirements. Without the necessary institutional adjustments, however, such an interim measure will not bring about any substantial changes in the problems existing generally with regard to judicial review in China.

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524 It was issued on 27 August 2002 and entered into force on 1 October 2002.

525 Article 9, Rule of International Trade Administrative Cases.

526 Article 5, Rule of International Trade Administrative Cases.

527 Guoguang Li's speech at the press meeting for the promulgation of 'Rule of the Supreme People's Court on Certain Issues Related to Hearing the International Trade Administrative Cases', 29 August 2002. Hongliu Gong, *Detailed Analysis of Judicial Interpretation on International Trade Administrative Cases*, Law Press, July 2003.

### 4.5.2 Judicial Review in Anti-Dumping Administration

The WTO specifically requires each member whose national legislation contains provisions on anti-dumping measures to maintain judicial, arbitral or administrative tribunals or procedures for the prompt review of administrative action relating to final determinations in anti-dumping cases.[528] China's first anti-dumping law was issued in 1997, and this makes no provision for judicial review. With the increase in anti-dumping proceedings initiated by China, foreign exporters whose products may be subject to dumping investigations urgently need a specialized judicial review provision. In 2004, the revised Anti-dumping Regulation[529] provided the first judicial review mechanism for anti-dumping determinations in China. Under Article 53 of the Anti-dumping Regulation, any interested party that refuses to accept the final ruling on whether to impose the anti-dumping duty may either apply for an administrative reconsideration in accordance with the law, or institute proceedings in a people's court.[530]

A Supreme People's Court's rule[531] also provides for a detailed and specific procedure for judicial review of anti-dumping decisions. The defendants in anti-dumping judicial review cases are mainly administrative authorities, such as the Ministry of Commerce and the Customs Tariff Commission of the State Council. Similar to the Rule of International Trade Administrative Cases, the judicial review of dumping determinations will be conducted by courts with higher hierarchy than those in normal judicial review cases. The first instance of these cases can either be conducted by a high people's court in the defendant's venue, or an intermediate people's court designated by the High Court.[532] The special provisions attempt to provide basic safeguards of procedural due process for foreign exporters, even though the problems existing in China's judiciary may still affect the protection for foreign exporters in the anti-dumping regime.[533]

### 4.5.3 Case Study – Judicial Review of Customs Valuation

A case study of a customs valuation review case can shed some light on whether these special provisions will in practice bring about improvements in foreign trade-related judicial review. The plaintiff, Foreign Trade Development Company of Zhaoqing City Guangdong

528 Article 13, Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade.

529 Anti-dumping Regulation of the People's Republic of China, issued by the State Council and revised in March 2004.

530 Article 53, Anti-dumping Regulation of People's Republic of China.

531 'Rule of the Supreme People's Court on Certain Issues Related to Application of Law in Hearings of Antidumping Administrative Cases', adopted by the Supreme People's Court, January 2003.

532 Article 5, 'Rule of the Supreme People's Court on Certain Issues Related to Application of Law in Hearings of Antidumping Administrative Cases'.

533 For the detailed analysis, see M. Ulric Killion, 'Quest for Legal Safeguard for Foreign Exporters under China's Anti-dumping Regime', *North Carolina Journal of International Law and Commercial Regulations*, Spring 2004.

province (Zhaoqing Foreign Trade Company), refused to accept the customs valuation made by the defendant, the Customs of Zhaoqing city (Zhaoqing Customs), and requested a judicial review at the Intermediate Court of Zhaoqing City.[534] In June 2005, the Intermediate Court of Zhaoqing City upheld Zhaoqing Customs' original decision on the valuation of the goods imported by the plaintiff. The plaintiff did not accept the judgment and appealed against it at the High Court of Guangdong Province. In November 2005, the High Court rejected the appeal and upheld the first-instance ruling.

The valuation of the price of imported goods for customs purposes is essential for tariff collections and other charges or restrictions on imports based upon value. For importers, the process of estimating the value of a product at customs presents problems that can be as serious as the actual duty rate charged.[535] The WTO Agreement on Implementation of Article VII (Customs Valuation Agreement) aims mainly to preclude the use of arbitrary or fictitious customs values and to provide greater certainty and uniformity in the valuation process. Under this agreement, the customs value of imported goods shall be the transaction value or, in other words, the price actually paid or payable for the goods when sold for export to the country of importation. This emphasizes that the basis for valuation should, as far as possible, be the transaction value of the relevant goods. If the transaction value cannot be determined, the agreement provides another five methods of valuation: transaction value of the same products, transaction value of similar products, deductive value, computed value and reasonable value. These valuation methods are, however, subject to sequential application. This means that a method can be applied only if the value cannot be determined using the prior listed method.

The main dispute in this case involved two issues. Firstly, the Zhaoqing Customs refused to accept the transaction value claimed by the plaintiff on the grounds that the plaintiff (importer) and the exporter were related. According to the Customs Valuation Agreement and the relevant Chinese legislation,[536] the fact that the buyer and seller are related shall not in itself constitute grounds for regarding the transaction value as unacceptable. If the Customs administration has grounds for believing that the relationship influenced the transaction value, it shall communicate the grounds to the importer and the importer shall be given a reasonable opportunity to respond.[537] The plaintiff disagreed with the Zhaoqing

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534 Case source: *Zhaoqing Foreign Trade Company* vs. *Zhaoqing Customs on Customs Valuation*, Rulings of High of Guangdong Province, issued on 24 November 2005, The Supreme People's Court Bulletin, No. 5, 2006.

535 Custom Valuation Gateway, http://www.wto.org/english/tratop_e/cusval_e/cusval_e.htm.

536 Provisions on the Customs of the People's Republic of China on Assessment of Duty on Import and Export Goods, issued by the General Administration of Customs of the People's Republic of China, on 28 March 2006, which replaced the old version issued on 31 December 2001.

537 Articles 48 and 49, Provisions of the Customs of the People's Republic of China on Assessment of Duty on Import and Export Goods. These Articles require the Customs to issue a 'Notice of Price Query' to duty payers and to consult with duty payers thereafter..

Customs' finding that there was such a relationship which would preclude the Customs from accepting the transaction value. It also claimed that if the Customs found there to be such a relationship, they should, as required by law, prove that the relationship influenced the transaction value.

However, the Zhaoqing Customs failed to prove that influence and refused the transaction value merely by the fact of the existence of the relationship. The Customs also refused to accept the information and materials provided by the plaintiff, which could have proved the transaction value to be acceptable. The Customs argued that the information and materials provided by the plaintiff could not be accepted since they contained many 'flaws and self-contradictions'. In the judicial review, the first-instance court supported the Customs' reasoning. It ruled that although the plaintiff tried to prove the transaction value was reasonable and authentic, the evidence itself was not reasonable and authentic because it contained various flaws and self-contradictions. The court also ruled that:

> The Customs, as a specialized administration authority on prices of import and export goods, obtains abundant information. Compared to the information provided by the plaintiff, the Customs' information is more authentic, and therefore, shall be adopted. The Customs found that the transaction value claimed by the plaintiff is lower than the comparable price of the same products, lower than the price reported by the international authentic website of similar products, and lower than the production costs. Based on this information owned by the Customs, the decision of the Customs that the transaction value has been influenced by the relationship is correct.

It seems that the court simply accepted the Customs' decision on the grounds of Customs being the administration authority and, therefore, having authentic information; the decision based on authentic information was automatically considered correct. Not being based on the facts or legal reasoning, the court justified the Customs' decision by virtue, at least partially, of Customs being an 'authority in customs administration'. In this argument, it is hard to see how the court can preclude arbitrary decisions by Customs. This ruling also contains an obvious contradiction with the other rulings discussed below.

Secondly, if the transaction value cannot be accepted, why did the Customs skip the other four sequential methods and directly adopt the last method (reasonable method) for the valuation? The only explanation provided by the Customs was that the plaintiff did not provide any information, and the Customs did not have the information needed to apply any of the other methods. As mentioned above, the relevant law states that if the transaction value cannot be accepted, the next method to be applied will be the transaction value of a product of the same type. It is only if the other four methods cannot be applied that the customs value can be determined using reasonable means according to the general principles and provisions of customs valuation regulations. The Customs claimed that it did not have information on the transaction value of the same products.

However, it contradictorily claimed that 'according to the abundant information owned by the Customs, the transaction value is lower than the comparable price of the same product'. The Customs used this information as the basis for doubting, and simultaneously proving, that the transaction value was influenced by the relationship. The obvious contradiction was completely ignored by the court. The court, without any analysis, ambiguously concluded that 'considering that the plaintiff did not provide necessary information, the Customs' adoption of the reasonable method, after excluding the other methods one by one, is legal and consistent with the due process requirement. Thus, the Customs decision shall not be regarded as *ultra vires*'.

In this case, the court played a negligible role in correcting inappropriate administrative action by the Customs. It failed to address obvious contradictions and omissions in the Customs' decision. Without the necessary analysis and legal reasoning, it reached its conclusion that the Customs decision was reasonable and legal. The special legislation for foreign trade-related judicial review cases promotes the first-instance court from the primary to the intermediate court. However, in the absence of the necessary institutional adjustments, neither the intermediate court nor even a high court can make judicial review a more effective mechanism for preventing arbitrary administrative decisions. Whether the idea of 'designing something special for the foreign trade regime' can provide additional protection for foreign traders is doubtful, and its real effect remains to be tested in future cases.

## 4.6 CONCLUSION

Unjustifiable subordination of judicial organs to political and administrative organs constitutes an institutional obstacle to independent judicial review in China. The lack of judicial independence not only tolerates external interference from governmental authorities and Party organs, but also induces self-restraint in the court in order to avoid confrontation with administrative authorities, particularly in judicial review cases challenging those administrative authorities. The extraordinary high withdrawal rate in judicial review litigation, which can be partially attributed to courts seeking to persuade plaintiffs to drop their case, strongly suggests an imbalance of power between the court and administrative authorities. Such an institutional limitation hinders judicial review in China from becoming an effective mechanism that provides a remedy for individuals, as desired by the WTO.

The limited scope of judicial review also exacerbates the problem caused by the institutional obstacle. It technically hinders the court from providing an effective and impartial review of specific administrative decisions. In many cases, reviewing the legality of administrative decrees on which specific administrative decisions are based is essential in order to review the legality of administrative decisions. If courts cannot revoke problematic administrative

decrees at local levels, these decrees will probably remain in effect and continue to infringe individuals' rights in the context of China's existing ineffective legislative review system.

The limited scope of review also impedes fulfillment of another function required by the WTO, i.e. uniform administration in implementation of law. The WTO rules have to be incorporated into national law in order to become binding at the domestic level. However, national-level law in China cannot adequately account for local circumstances. The consistency of local rules and their implementation by administrative authorities constitute a key factor in the uniform application of national-level law. Through judicial review, the court is in the best position to administer better compliance. Thus, higher-level courts should be empowered to reach effective decisions by, where necessary, striking down local regulations at lower levels if these conflict with superior laws. If institutional reform is not feasible in the short term, expanding the scope of review, through a much more technical reform, may alleviate the problem of judicial review in China.

China has implemented a series of judicial reforms. The Office of Reviewing and Recoding Law and Regulation, for example, was specifically established under the SCNPC in 2004 to conduct preliminary reviews of conflicts between inferior law and superior law or the Constitution; centralization of court funding at all levels in China was incorporated into the new agenda of judicial reform in 2008 so as to minimize local courts' reliance on local governments and to enhance their independence; efforts have also been made to improve the judicial review, especially for foreign trade-related cases. These measures are mostly technical improvements, which could bring about some short-term effects. Within the existing institutional framework, however, the effects in terms of establishing independent judicial review and promoting the rule of law in the longer term are limited. Enhancing judicial authority and independence, as the part of holistic institutional reform, is the key to improving the effectiveness of judicial review in China.

# Chapter 5

## Intellectual Property Rights Enforcement in China—Case Study

## 5.1 INTRODUCTION

The purpose of this chapter is to demonstrate how institution-related difficulties found in the areas of transparency, uniform administration of application of law and judicial review may impede China's compliance with the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) enforcement requirements. If the previous chapters examine how those difficulties hinder China's compliance with WTO obligations at an abstract level, this chapter, by focusing on the compliance with a much more substantive WTO obligation, shows how these difficulties hinder China's compliance at a concrete level. It exemplifies the importance of WTO systemic obligations provided in GATT Article X as *sine qua non* for the effectiveness of WTO substantive obligations.

No set of WTO compliance difficulties illustrate the basic dynamics of institutional impediments faced by China better than those in IPR enforcement. Western attempts to obtain Chinese compliance with intellectual property rights (IPR) have a long history of failure.[538] Protection of IPR thus became one of the most formidable obstacles in the negotiations of China's WTO accession. China has undertaken strenuous efforts to adapt model intellectual property laws from the US and Europe[539] and to bring its domestic legal system of intellectual property protection into conformity with the WTO requirements. Upon WTO accession, it was generally accepted that the gap between the TRIPS agreement and

538 John Alan Lehman, Intellectual Property Rights and Chinese Tradition Section: Philosophical Foundations, *Journal of Business Ethics*, 69:1-9, 2006. Of all the foreign players affecting China's intellectual property protection system, the Americans are probably the most vocal and aggressive. In order to eliminate piracy problems in China, US conducted bilateral negotiations with China since the beginning of 1990s and signed three bilateral intellectual property agreements in 1992, 1995 and 1996 respectively. Although China's efforts to enhance intellectual property protection after the bilateral negotiations and the improvements achieved have been recognized, US policies in these bilateral agreements were deemed largely ineffective with regard to the remaining widespread IP-infringing activities in China. The bilateral agreements have been regarded as 'cycle of futility'. Peter K. Yu, 'Still Dissatisfied after All These Years: Intellectual Property, Post-WTO China, and the Avoidable Cycle of Futility', *Georgia Journal of International and Comparative Law*, vol. 34, 2006; Ryan P. Johnson, 'Steal this Note: Proactive Intellectual Property Protection in the People's Republic of China', Connecticut Law Review, vol. 38, p. 1036, 2006.

539 Deli Yang, *Intellectual Property and Doing Business in China*, Emerald Group Publishing, 2003; John Alan Lehman, 2006; Qingjiang Kong, 'Judicial Enforcement of Intellectual Property Rights in China on the Eve of WTO Accession', in Qingjiang Kong (ed.), *WTO, Internationalization and the Intellectual Property Rights Regime in China*, Marshall Cavendish Academic, 2005, p. 45.

Chinese intellectual property (IP) laws had been greatly narrowed,[540] and that, technically, Chinese IP laws as a whole were adequate for the prevention of IPR infringements.[541]

In the years since China's WTO accession, however, protection of IPR has been a constant source of complaints from other WTO members. Counterfeiting and piracy[542] remain out of control and China is still considered to be one of the world's largest exporters of fake goods.[543] Despite the IP laws being largely compatible with TRIPS, China has been unable to enforce those laws effectively. Much has been done in an effort to eradicate the problem, but rampant IPR infringements have become a perennial problem.[544] A broad consensus is developing that it is enforcement rather than legislation that is hindering China from ensuring effective protection of IPR. In other words, the main problem in IPR protection in China is not the fact that the laws are lacking, but rather that the country lacks the effective mechanism and institutions needed to enforce the laws.[545] Thus, a study of the problematic IPR enforcement, epitomizing the institution-related problems in the enforcement mechanism, provides a perfect example of the institutional barriers in China's compliance with WTO systemic obligations.

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540 See, for example, Robert Bejesky, 'Investing in the Dragon: Managing the Patent Versus Trade Secret Protection Decision for the Multinational Corporation in China', 11 *Tulsa Journal of Comparative and International Law*, 2004; Wei Shi, 'Incurable or Remediable? Clues to Undoing the Gordian Knot Tied by Intellectual Property Rights Enforcement in China', 30 *University of Pennsylvania Journal of International Law*, 2008; Warren Newberry, 'Copyright Reform in China: A "TRIPS" Much Shorter and Less Strange than Imagined?', 35 *Connecticut Law Review,* 2003.

541 Wei Shi, 2008.

542 Counterfeit goods are those that bear a mark that is identical, or virtually identical, to a registered trademark without authorization, in violation of the trademark owner's intellectual property right. Piracy, a related practice, may be defined as any unauthorized duplication of intellectual property that violates an intellectual property right. Ryan P. Johnson, 2006, p. 1036.

543 Robert Marquand, China's Pirate Industry Thriving, *The Christian Science Monitor*, 9 January 2002, available at http://www.csmonitor.com/2002/0109/p6s1-wosc.html; International Intellectual Property Alliance, 2004 Special 301 Report: People's Republic of China, 2004, noting that 90% of all IP-protected goods sold in China have been counterfeited or illegally copied. See also Daniel Chow, 'Anti-Counterfeiting Strategies of Multi-National Companies in China: How A Flawed Approach Is Making Counterfeiting Worse', *Georgetown Journal of International Law*, vol. 41, No. 4, 2010.

544 Wei Shi, 2008.

545 Brent T. Yonehara, 'Enter the Dragon: China's WTO Accession, Film Piracy and Prospects for the Enforcement of Copyright Laws', *UCLA Entertainment Law Review*, No. 9, Spring 2002.

The perennial problem of China's IPR enforcement[546] make it interesting to question whether China has been found, by the WTO DSB, TRIPS incompliant. The institution-related difficulties may, or may not, lead to a failure in the fulfillment of TRIPS obligations against the standards established by the WTO DSB. As it is discussed in Chapter one, the institution-related difficulties may affect more in the process of 'compliance' (*de facto* adherence to domestic measures that are adopted for implementing international agreements) than in the process of 'implementation' (adoption of domestic measures to incorporate obligations in international agreements) , while the WTO DSB may focus only on the 'implementation'. In order to clarify whether China is deemed as TRIPS incompliant, Part II of this chapter examines carefully on the text of enforcement provisions of the TRIPS and the panel report on the first and only China's IPR dispute. It demonstrates that there could be a substantial gap between the standard of 'implementation' and 'compliance' due to the institution-related difficulties in the process of enforcement. Part III briefly introduces various IPR enforcement mechanisms adopted in China. Part IV, V and VI examine respectively how the problems existing in transparency, uniform administration of application of law and judicial review may hinder effective IPR enforcement in China. Part VII concludes.

## 5.2 TRIPS ENFORCEMENT PROVISIONS AND CHINA'S COMPLIANCE

Over the past two decades or so, China has demonstrated a strong desire and concerted efforts to establish a sound legal framework in order to enhance IPR protection in line with the TRIPS requirements. Problems continue to exist, however, mainly in IPR enforcement.[547] The perennial problem in China's IPR enforcement makes it necessary to question whether or the extent to which China complies with TRIPS obligations. The alleged failure for China to

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546 There is extensive literature discussing the obstacles to China's IPR enforcement from various aspects, including i) cultural and philosophical impediments; see, for example, John Alan Lehman, 2006; Jordana Cornish, 'Cracks in the Great Wall: Why China's Copyright Law Has Failed to Prevent Piracy of American Movies Within its Borders', *Vanderbilt Journal of Entertainment and Technology Law*, vol. 9, No.2, 2006; ii) limitation of the level of economic development , such as low average income, low innovation capacity, China as a net importer of IPR goods and services; see, for example, Mark Liang, 'A Three-Pronged Approach: How the United States Can Use WTO Disclosure Requirements to Curb Intellectual Property Infringement in China', *Chicago Journal of International Law*, summer 2010; Kim F. Natividad, 'Stepping It Up and Taking It To the Streets: Changing Civil and Criminal Enforcement Tactics, No. 23, *Berkeley Technology Law Journal*, 2008; iii) political and policy concerns, which are mainly about the government's priority-setting with regard to IPR protection; see, for example, William Alford, *To Steal A Book is An Elegant Offense: Intellectual Property Law in Chinese Civilization*, Stanford University Press, 1997; iv) problems of judicial system; see, for example, Qingjiang, Kong, 'Judicial Enforcement of Intellectual Property Rights in China: on the Eve of WTO Accession', *The Journal of World Intellectual Property*, vol. 4, 2001.

547 A broad consensus is developing that it is enforcement rather than legislation that prevents China from fulfilling its TRIPS obligations. Peter Ganea and Thomas Pattloch (eds.), *Intellectual Property Law in China*, Kluwer Law International, 2005.

fulfill its obligations under the TRIPS[548] needs to be tested based on a carful examination of the precise meaning and interpretation of TRIPS obligations (for the purpose of this chapter TRIPS obligations on enforcement).

### 5.2.1 TRIPS Diagnosis – Ambiguous Enforcement Provisions

The TRIPS Agreement was intended to satisfy IP-dependent nations' concerns about the lack of intellectual property protection under GATT.[549] The increased importance of intellectual property-dependent goods to the US economy motivated the United States to advocate an international standard for protecting IPR during the Uruguay Round.[550] It was believed that the international venue for protecting these rights at that time, the World Intellectual Property Organization (WIPO), was ineffective because it could not impose any real punishment, such as trade sanctions, upon infringers.[551] Other countries opposed a heightened standard of IPR protection and harsher punishment for infringers, labeling such provisions as protective of countries that developed and exported intellectual property (i.e. developed countries) and detrimental to developing nations.[552] After much negotiation and compromise, a minimum international standard for IPR protection was created in the form of the TRIPS Agreement. The Agreement incorporates and builds upon a range of provisions contained in several pre-existing international IP conventions.[553]

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548 See for example, Tobias Bender, 'How to Cope with China's (Alleged) Failure to Implement the TRIPS Obligations on Enforcement', *The Journal of World Intellectual Property*, Vol. 9, Issue 2, March 2006, pp. 230-250; Frederick M. Abbott, 'China in the WTO 2006: 'Law ad its Limitations' in the Context of TRIPS', in Bermann, P. Mavroidis eds., *WTO Law and Developing Countries*, Cambridge University Press, 2007, pp.59-81.

549 Glen T. Schleyer, Power to the People: Allowing Private Parties to Raise Claims Before the WTO Dispute Resolution System, *Fordham Law Review*, vol. 65, 1997; Ryan P. Johnson, 2006.

550 US and Japan proposed to cover all IPR and enforcement, not just trademark goods. Daniel Gervais, *The TRIPS Agreement: Drafting History and Analysis*, 3rd edition, Thomson Routers, 2008; Warren Newberry, 'Copyright Reform in China: A "TRIPS" Much Shorter and Less Strange Than Imagined?', *Connecticut Law Review*, 2003, noting the increased US dependence on high-tech goods in the 1980s and its efforts at the Uruguay Round to create a supranational agreement on IPR protection.

551 Warren Newberry, 2003, noting that the WIPO dispute resolution mechanism relied on the voluntary cooperation of parties and thus could not impose any real punishment, such as trade sanctions, on problem nations.

552 For instance, Brazil and Argentina opposed inclusion of IPR in a new round. Daniel Gervais, 2008; Warren Newberry, 2003, noting that developing countries opposed TRIPS on the grounds that it favored developed nations at the expense of developing nations, forcing them to overhaul legal systems and implement costly legislation that would ultimately prevent them from reaping the rewards of appropriating developed nations' IPR.

553 TRIPS encompasses four major international intellectual property agreements: the Paris Convention for the Protection of Industrial Property; the Berne Convention for the Protection of Literary and Artistic Works; the Rome Convention for the Protection of Performers, Producers of Phonograms, and Broadcasting Organizations; and the Treaty on Intellectual Property in Respect of Integrated Circuits.

One of the most notable features of TRIPS is that it is the first international covenant on IPR protection that includes enforcement provisions.[554] Twenty-one provisions, Article 41 to 61, are set to provide international minimum standards on the enforcement of intellectual property rights. These obligations are ranging from border measures to criminal sanctions. Members are required to adopt four basic procedures and to have remedies for IPR enforcement available in their domestic legal system (including civil, administrative and criminal procedures), as well as border measures.[555] TRIPS imposes an unprecedented set of obligations on governments to ensure that private IP rights holders can take 'effective action' against IP infringements. Specifically, it requires members to establish enforcement procedures that include 'expeditious remedies' to prevent infringements and provide remedies that constitute a 'deterrent' to further infringements.[556] Article 41.1 of TRIPS states that:

> Members shall ensure that enforcement procedures as specified in this Part are available under their law so as to permit effective action against any act of infringement of intellectual property rights covered by this Agreement, including expeditious remedies to prevent infringements and remedies which constitute a deterrent to further infringements.[557]

While the provisions on enforcement in TRIPS are significantly stronger and more specific than any prior international IP agreement, they are ambiguous and open-ended. Many of the key terms in the Agreement, such as 'effective action', 'expeditious remedies' and 'deterrent', are left undefined.[558] The number of disputes under this Article is limited, and the WTO DSB does not provide much explanation on the descriptions and definitions of

554 Tobias Bender, 'How to Cope with China's (Alleged) Failure to Implement the TRIPS Obligations on Enforcement', *The Journal of World Intellectual Property*, vol. 9, No. 2, pp. 230-250, 2006.

555 For the provisions on civil and administrative procedures, see TRIPS Agreement Articles 42-50; for the provisions on border measures, see TRIPS Articles 51-60; for the provision on criminal procedure, see TRIPS Article 61.

556 Article 41, TRIPS.

557 Article 41(1), TRIPS.

558 As for remedies, TRIPS Article 45 merely indicates that damages must adequately remedy the rights holder's injury. Article 46 expands on the concept of deterrent by requiring that, in order to create an effective deterrent to infringement, the authority shall be empowered to seize infringing goods and dispose of them outside the channel of commerce. It rejects the mere removal of an unlawfully affixed trademark and the subsequent release of goods into the channel of commerce as adequate action.

deterrent or expeditious remedies.[559] Moreover, although the TRIPS agreement ushered in new and higher standards on international intellectual property enforcement, these standards have yet to strengthen intellectual property enforcement to the satisfaction of developed countries. Many developed countries and their supportive industries consider these standards primitive, constrained, inadequate, and ineffective.[560]

The reason for the vagueness of the enforcement provisions of the TRIPS and its failure to develop stronger enforcement norms is related to the contest between developed countries and less developed countries in the negotiation process. Strong intellectual property enforcement requires a substantial investment of resources, the development of supporting institutional infrastructures, the introduction of complementary policy reforms, and intrusions upon a country's sovereignty. This challenge is particularly acute in less developed countries. As a result of the negotiation tactics developed by less developed countries, the TRIPS agreement now contains many result-oriented terms that are vague, broad, and undefined. Examples of these terms are " 'effective', 'reasonable', 'undue', 'unwarranted', 'fair and equitable', and 'not…unnecessarily complicated or costly' ". [561] Moreover, the inclusion of Part III of TRIPS contains only empowerment norms, as compared to norms that mandate specific actions.[562] For instance, Article 59 states that competent authorities shall have the authority to order the destruction or disposal of infringing goods

559 The panel made interpretations on TRIPS Article 41.1 only in two cases: European Communities—Protection of Trademarks and Geographical Indication for Agricultural Products and Foodstuffs, DS 174, 15 March 2005, and China—Measures affecting Protection and Enforcement of Intellectual Property Rights, DS 362, 26 January 2009. The Panel's interpretations are, however, not very helpful to clarify the meaning of the specific terms mentioned above. For example, the Panel emphasized in the former case that 'Article 41.1 imposes an obligation and it is not a hortatory, in response to the European Communities' claim that Article 41.1 is a purely a introductory provision which does not create separate legal obligations.' The Panel further stated that the substance of this Article added qualitative elements to the procedures specified in Part III through use of terms such as 'effective', 'expeditious', and 'deterrent' and it is not redundant. In the latter case, the Panel ruled that by simply not preventing right holders from filling and pursuing claims could not be viewed as sufficient enforcement procedures as required by this Part. 'Enforcement procedures as specified in this Part' were far more extensive, and China's entire ban on publication of a work could be considered neither as a form of 'effective action', nor as 'an alternative form of enforcement against infringement'. In these two cases, the Panel, rather than clarifying what constitute effective action or enforcement procedures required in Article 41.1, simply excluded some actions from 'effective action or enforcement procedures'.

560 Peter K. Yu, 'TRIPS and Its Achilles' Heel', *Journal of Intellectual Property Law*, vol. 18, pp. 479-531, 2011; See for example, European Community, Directorate General For Trade, *Strategy for the Enforcement of Intellectual Proeprty Righs in Third Countries* 3, 2005; Timothy P. Trainer and Vicki E. Allums, *Protecting Intellectual Property Rights Across Borders*, Thomason West, 2009.

561 U.N. Conference on Trade & Development—International Centre for Trade & Sustainable Development, *Resource Book on TRIPS and Development*, 2005; J.H. Reichman, 'Universal Minimum Standards of Intellectual Property Protection Under the TRIPS Component of the WTO Agreement', in Carlos M. Correa and Abdulqawi A. Yusuf eds., *Intellectual Property and International Trade*, Kluwer Law International, 2nd edition, 2008, p. 23, 71.

562 TRIPS Agreement, Article 43-48, 50, 53, 56, 57, 59.

seized at the border. This provision requires only the provision of authority, but not the exercise of such authority in a specified way.

If weakening of TRIPS language was not enough, less developed countries successfully demanded the inclusion of limitations and exceptions in the TRIPS.[563] The most notable exception in the enforcement area is Article 41.5, which states explicitly that a WTO member is not required to devote more resources to intellectual property enforcement than to other areas of law enforcement. Article 1.1 also provides that members shall be free to determine the appropriate method of implementing the provisions of this agreement within their own legal system and practice. Less developed countries specifically demanded this provision to alleviate concerns about the lack of resources needed to set up specialized intellectual property courts or to strengthen intellectual property enforcement.[564] Even today, less developed countries continue to insist that Article 41.5, along with Article 1.1, represents the key concessions they won through the TRIPS negotiation process.[565]

In order to reconcile the differing interests of developed and developing nations, TRIPS incorporates empowerment norms and principles statements in its enforcement provisions. The margin of policy flexibility in the enforcement was left for developing countries. While developed countries successfully pushed for the inclusion of their preferred standards in the TRIPS agreement, less developed countries were able to inject ambiguities, flexibilities, limitations and exceptions into the Agreement.[566] The adoption of Article 41 to 61 on enforcement provisions undeniably has helped the developed countries to begin the norm-setting process. However, the TRIPS is apparently far from a final deal.[567] Rather, it is the starting point for further negotiations on greater norm development.[568]

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563 Peter K. Yu, 'TRIPS and Its Achilles' Heel', *Journal of Intellectual Property Law*, vol. 18, pp. 479-531, 2011.

564 Carlos M. Correa, *Trade Related Aspect of Intellectual Property Rights: A Commentary on the TRIPS Agreement*, Oxford University Press, 2007, p. 417; U.N. Conference on Trade & Development—International Centre for Trade & Sustainable Development, *Resource Book on TRIPS and Development*, 2005; Peter K. Yu, 'TRIPS and Its Achilles' Heel', *Journal of Intellectual Property Law*, vol. 18, pp. 479-531, 2011.

565 For example, China made this claim in the TRIPS enforcement dispute settled in 2009. Panel Report, China-Measures Affecting the Protection and Enforcement of Intellectual Property Rights, WT/DS362/R, 26 January, 2009, Annex B-4, 33, ("Article 1.1 and 41.5 were key concessions to the developing world, which the United States and other developed third parties seek now to dismiss and disregard."); Peter K. Yu, 'TRIPS and Its Achilles' Heel', *Journal of Intellectual Property Law*, vol. 18, pp. 479-531, 2011.

566 Peter K. Yu, 'TRIPS and Its Achilles' Heel', *Journal of Intellectual Property Law*, vol. 18, pp. 479-531, 2011.

567 Carolyn Deere, *The Implementation Game: The TRIPS Agreement and the Global Politics of Intellectual Property Reform in Developing Countries*, Oxford University Press, 2009, p. 304.

568 Carolyn Deere, *The Implementation Game: The TRIPS Agreement and the Global Politics of Intellectual Property Reform in Developing Countries*, Oxford University Press, 2009, p. 304.

### 5.2.2 Panel Report on China's IPR enforcement case

The flexibilities provided by TRIPS might be necessary for it to become a multinational accepted framework for IPR protection. However, the flexibilities and ambiguities may hinder the TRIPS in proving effective global intellectual property enforcement. As mentioned above, the DSB's application and interpretation on TRIPS enforcement provisions are quite limited. It will be difficult to have an assessment on members' compliance with TRIPS obligations if the enforcement provisions are vague and undefined. The dispute between China and US settled in 2009, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, is important in that the panel, for the first time, focused primarily on the interpretation and implementation of the TRIPS enforcement provisions. Since the text of TRIPS enforcement provisions are not straightforward, it is necessary to examine this panel report, which might be useful to answer the questions on what would be considered sufficient to be TRIPS compliant and whether China is compliant or not.

#### *Panel's findings in three claims*

In August 2007, the US requested the DSB to establish a panel to examine three claims against China regarding its failure to protect and enforce intellectual property rights pursuant to the TRIPS. The first claim concerned the thresholds for criminal procedures and penalties. Because WTO member is required to apply criminal procedures and penalties to all cases involving 'willful trademark counterfeiting or copyright piracy on a commercial scale', according to Article 61 of the TRIPS, the US claimed that China had failed to honor its TRIPS commitments by including in its law high thresholds for applying criminal procedure and penalties to intellectual property infringement.[569] As a result, in the US's view, the high threshold provided a safe harbor to shelter pirates and counterfeiters from criminal prosecution.[570]

According to the panel, the key in deciding this claim is the precise meaning of Article 61, especially the definition of infringements 'on a commercial scale'. Although the term 'commercial scale' was 'intentionally vague… and left undefined' in the TRIPS agreement,[571] the panel noted that the term was adopted out of a 'deliberate choice' and therefore 'must be given due interpretative weight.'[572] The panel further noted that the term provides 'a relative standard, which will vary when applied to different fact situations.'[573] It found

569 Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, p.731.

570 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.494.

571 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, Annex B-1, paragraph 22.

572 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.543.

573 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.600.

that the term meant 'the magnitude or extent of typical or usual commercial activity with respect to a given product in a given market.' To assess the consistency of China's criminal thresholds with this complex definition, the panel looked to specific conditions in China's marketplace. Although the US provided evidence in the form of press articles and industry and consultant reports,[574] the panel found the evidence insufficient to demonstrate what constituted a commercial scale in the specific situation of China's marketplace.[575] The information is inadequate to demonstrate what is typical and usual in China for the purpose of the relevant treaty obligations.[576] The panel did not endorse China's thresholds but concluded that the factual evidence presented by the US was inadequate to show whether or not the cases excluded from criminal liability met the TRIPS standard of 'commercial scale' when that standard is applied to China's marketplace.[577] In sum, without determining whether China has satisfied its TRIPS obligations, the WTO panel found that the US had failed to substantiate its claim.

The second claim concerned whether Chinese customs authorities properly dispose of infringing goods seized at the border. Article 59 of the TRIPS provides that competent authorities shall have the authority to order the destruction or disposal of infringing goods in accordance with the principles set out in Article 46 of the TRIPS. Those principles emphasize that infringing goods shall be able to be disposed outside the channels of commerce in such a manner to avoid any harm caused to the right holder, in order to create an effective deterrent to infringement.[578] The US complained that China introduced a 'compulsory scheme' that took away the ability of the customs authorities to exercise their discretion to order destruction or disposal of infringing goods.[579] This scheme precluded the authorities form destroying the infringing goods unless they found it inappropriate to donate the goods to charities, sell them to right holders, or auction them off after eradicating the infringing features.[580] The panel did not find any inconsistency of donation and sales to right holders

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574 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.615-7.616.

575 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.614.

576 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.629.

577 Key findings of the dispute, available at http://www.wto.org/english/tratop_e/dispu_e/cases_e/1pagesum_e/ds362sum_e.pdf

578 TRIPS, Article 46 states that in order to create an effective deterrent to infringement, the judicial authorities shall have the authority to order that goods that they have found to be infringing be, without compensation of any sort, disposed of outside the channels of commerce in such a manner as to avoid any harm caused to the right holder, or, unless this would be contrary to existing constitutional requirement, destroyed.

579 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.197.

580 Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, p.736.

for the reason that the remedies specified in Article 59 are not exhaustive.[581] However, the panel faulted China for the way its customs authorities auctioned off the seized goods.[582] Although auctioning of goods in not prohibited by Article 59, the panel concluded that the way in which China's customs auctions these goods was inconsistent with Article 59, because it permit the sale of goods after the simple removal of the trademark in more than just exceptional cases.[583] In sum, China lost part of the second claim. Even though the panel upheld as TRIPS-consistent the use of donations, sales to rights holders and auctions, the way in which China auction the infringing goods is inconsistent with TRIPS requirement.

The panel's finding in the third claim is comparatively more straightforward. It concerned Article 4 of the Chinese Copyright Law, which states that 'works the publication and /or dissemination of which are prohibited by law shall not be protected by this Law.' It means China denies copyright protection to the works that are banned by other Chinese laws, such as Criminal Law, Regulations on the Administration of Publishing Industry, and Regulations on the Administration of Broadcasting, etc. While the panel recognized a country's sovereign right to censor, it pointed out that 'copyright and government censorship address different rights and interests.'[584] In the panel's view, censorship regulations cannot eliminate rights that are inherent in a copyrighted work.[585] The panel found that while China has the right to prohibit the circulation and exhibition of works, as acknowledged in Article 17 of the Berne Convention, this does not justify the denial of all copyright protection in any work.[586] China's failure to protect copyright in prohibited works (i.e. that are banned because of their illegal content) is therefore inconsistent with Article 5 (1) of the Berne Convention as incorporated in Article 9.1, as well as with Article 41.1, as the copyright in such prohibited works cannot be enforced.[587] China lost the third claim.

### *Article 41.5 and Article 1.1—justification for non-compliance?*

As discussed above, TRIPS leaves some policy space flexibilities for less developed countries. The inclusion of Article 1.1 and Article 41.5 are the most representative examples of the

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581 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.327.

582 Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, p.738.

583 Key findings of the dispute, available at http://www.wto.org/english/tratop_e/dispu_e/cases_e/1pagesum_e/ds362sum_e.pdf

584 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.135.

585 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.135; Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, p.742.

586 Key findings of the dispute, available at http://www.wto.org/english/tratop_e/dispu_e/cases_e/1pagesum_e/ds362sum_e.pdf

587 Key findings of the dispute, available at http://www.wto.org/english/tratop_e/dispu_e/cases_e/1pagesum_e/ds362sum_e.pdf

possible limitations to TRIPS obligations. The third sentence of Article 1.1 provides that 'members shall be free to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice.' It echoes the Agreement's preamble, which recognized 'the special needs of the least-developed county members in respect of maximum flexibility in the domestic implementation of laws and regulations on order to enable them to create a sound and viable technological base.'

In this dispute, China invoked Article 1.1 in its response to the US's complaint over China's use of criminal threshold. It claimed that this provision laid down a specific caveat that establishes boundaries on obligations, specifically in the realm of enforcement.[588] However, the panel rejected China's position. While the panel agreed that differences among members' respective legal systems and practices tend to be more important in the area of enforcement, Article 1.1 does not permit those differences to justify any derogation from the basic obligation to give effect to the provisions on enforcement.[589] Instead of allowing a member state to lower the specified TRIPS standards, the provision merely grants to a WTO member freedom to determine the appropriate method of implementation of the provisions.[590]

The panel's interpretation of Article 1.1 is consistent with that found in the reports of the AB or other WTO panels.[591] Similar interpretation includes 'while the WTO members are free to choose the method of implementation, the minimum standards of protection are the same for all of them.' In all of these reports, no respondent has ever succeeded in using the third sentence of Article 1.1 to defend its measures against non-compliance with the TRIPS obligations. It is fair to assume that the future use of this Article is unlikely to provide any effective defense against TRIPS noncompliance, even though WTO members may still tempted to include such a sentence in their oral statements or written submissions.[592]

What the DSB emphasizes in the interpretation is that flexibility does not permit derogation from TRIPS obligations. It may make third sentence of Article 1.1 difficult to be viewed as a 'special clause' for less-developed countries. It disappoints less-developed countries since it goes against the original intention to include such an Article by those countries, i.e. 'international conventions on intellectual property protection incorporated the freedom of member states to attune their intellectual property protection system to their own needs

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588 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.511.

589 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.513.

590 Panel Report, *China—Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R, January 26, 2009, paragraph 7.513.

591 For detailed discussion, see Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, pp.774-778.

592 Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, p.776.

and conditions.'[593] How this article is prohibited to be used as justification for non-compliance for developing countries is obvious. But how it could be used as a flexibility provision to take the 'special needs' of developing countries into account remains to be seen.
Another article that has also been viewed as key concession to the developing world in the TRIPS agreement is Article 41.5. It provides that:

> 'It is understood that this Part (Part III on enforcement) does not create any obligation to put in place a judicial system for the enforcement of intellectual property rights distinct from that for the enforcement of law in general, nor does it affect the capacity of members to enforce their law in general. Nothing in this Part creates any obligation with respect to the distribution of resources as between enforcement of intellectual property rights and the enforcement of law in general.'

This provision states explicitly that a WTO member is not required to devote more resources to intellectual property enforcement than to other areas of law enforcement. It limits intellectual property enforcement obligations to what is achievable in light of the resources for the general law enforcement. Moreover, this article does not create any obligation to affect the capacity of members to enforce their law in general. The provision is particularly important to less developed countries, who were deeply concerned about the need to reallocate a considerable amount of resources to set up specialized intellectual property courts of strengthen intellectual property enforcement. For this reason, less developed countries specifically demanded the inclusion of Article 41.5 in the TRIPS.[594]
In this dispute, China referred to Article 41.5 and speculated that defining a crime with too low threshold 'could unleash a large volume of private enforcement actions and imposes a significant burden on the judicial system'. The argument based on this Article would be of great significance to China and as well as other less-developed countries that are facing resources and capacity constraints in intellectual property enforcement. Unfortunately, however, the panel in this dispute did not give much interpretation on the application of Article 41.5 in response of China's argument. It only stated that China was unable to substantiate its concern regarding how the low threshold would have overburdened its criminal law system. In particular, China lacked any data relevant to its experience after it lowered threshold for the crimes infringing intellectual property rights in 2004. Therefore, the panel did not need to consider this issue further.
Although the panel did not make further interpretation on this Article, it is possible to notice a difference between how the panel treats Article 41.5 and Article 1.1. The panel did not explicitly declare that Article 41.5 does not permit the use of resource constraints 'to justify

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593 Negotiating Group on Trade-related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods, Note by the Secretariat: Meeting of Negotiating Group of 12-14 July, 1989, paragraph 5, MTN. GNG/NG11/14.

594 U.N. Conference on Trade & Development—International Centre for Trade & Sustainable Development, *Resource Book on TRIPS and Development*, 2005; Peter K. Yu, 'TRIPS Enforcement and Developing Countries', *American University International Law Review*, vol. 26, 2011, p.779.

any derogation from the basic obligations' of TRIPS—the wording used in the interpretation of Article 1.1. At least, the panel did not exclude the possibility for using 'resource constraints' to justify derogation from TRIPS enforcement obligations in future cases if members can substantiate their claims with sufficient evidences. If China could prove, for example in this case, that lowering threshold for intellectual property criminal liability makes resource demands in the area of intellectual property enforcement far exceed those in other areas of law enforcement, China might have chance to prevail.

In sum, although Article 1.1 and Article 41.5 leave the margin of policy flexibility for developing countries, they have hardly been used as successful justification for any non-compliance in practice. Article 1.1 allows members to determine the appropriate method of implementation, but it does not allow members to lower the basic TRIPS standards. Article 41.5 limits the obligations to what is achievable in light of the resources of the general law enforcement, but whether the resource constraints can be used to justify derogation from the basic TRIPS obligations remains unclear. How or whether these provisions will play their due role in practice to take the special needs of developing countries into account needs to be tested in future WTO cases.

### *TRIPS Compliant or not—Limits of Panel Report and TRIPS Agreement*

In China's first and only IPR-related dispute, the panel found both consistencies and inconsistencies, half and half, in certain specific aspects of China's IPR enforcement with its obligations under the TRIPS. The panel's rulings clarify some terms of enforcement provisions and demonstrate that China's implementation of IPR enforcement seems to reach an acceptable level. The panel's rulings are, however, not helpful to answer the general question of whether or the extent to which China is TRIPS compliant. Neither does the text of TRIPS enforcement requirements, which is vague and undefined. As a matter of textual interpretation and the object and purpose of the TRIPS Agreement, a claim for failure to effectively enforce the TRIPS Agreement should be based on a systemic failure by China or an identifiable 'measure' that fails to be in conformity with TRIPS standards.[595] A panel or the AB would need to establish new standards under which to access a claim for failure to permit the effective enforcement of IPR.[596] What quantum of enforcement failures would constitute a systemic failure?[597] It will be an extremely difficult, if not impossible, mission for the DSB. The panel stated in its report of China's IPR dispute that,

> 'The Panel's task was not to ascertain the existence or the level of trademark counterfeiting and copyright piracy in China in general nor to review the desirability of strict IPR enforcement. … The Panel's mandate was limited to a review of whether

595 Frederick M. Abbott, 2007.
596 Frederick M. Abbott,2007.
597 Frederick M. Abbott, 2007.

those alleged deficiencies are inconsistent with those specific provisions of the TRIPS Agreement.'

Despite of the technical difficulties, the panel has explicitly stated that judging the level of China's compliance in general is not its task. The panel only reviews the consistency of specific provisions. Although a few inconsistencies have been found, it would be unreasonable to speculate, based on the panel's finding in this dispute, that there is serious incompliance of China's IPR enforcement regime with regard to the TRIPS obligations. It brings an odd contrast to the general sense of problematic China's IPR enforcement and the experiences of WTO members that face with constant complaints of dissatisfied IPR protection in China from intellectual property right holders.

This contrast raises an interesting question that why China, a country with the rampant counterfeiting and piracy, would not be found TRIPS incompliant by the WTO DSB. One possible explanation is that the panel only checks with the 'implementation' but not the 'compliance' of WTO members. As discussed in Chapter one, it means the panel only looks into the Chinese laws on their consistency with TRIPS obligations (the implementation step), but not the enforcement of the laws and the changes it could bring to IPR protection (the compliance step). When the deficiency of effective IPR protection comes mainly from the enforcement rather than the law themselves, it will be unlikely for the panel to find serious violations of China's performance. And even if it does, the change that the revision of Chinese IP laws could bring to IPR enforcement at practical level is skeptical. It would probably be undermined by the problems encountered in the process of enforcement. In effect, the panel's decision may lead to a better compliance for the sake of the consistency with the WTO's rules, but may not lead to a real change for the sake of the interests of WTO members and IP right holders. The limit of the panel's decision, as well as the TRIPS provisions, lies in the WTO's objective to strike a balance between what is achievable and what is desirable, and to preserve stability of the WTO system without placing more weight on the legal rules than what they can bear. Nonetheless, if the TRIPS and its enforcement by the WTO DSB would not enhance IPR enforcement in China to a minimum acceptable level, whether the TRIPS, or the WTO legal system, is capable of addressing China's intellectual property problem will be questioned.

The following sections of this chapter discuss how the institution-related difficulties found in fields of transparency, uniform administration of application of law, and judicial review, may hinder China's IPR enforcement. It explains, to certain extent, the problems in the process of IPR enforcement, and accordingly demonstrates why the gap between 'implementation' and 'compliance' could be substantial in China.

## 5.3 OVERVIEW OF CHINA'S IPR ENFORCEMENT MECHANISMS

China has adopted a multi-track system for IPR enforcement, under which interested parties may seek to resolve IP-related disputes through administrative procedures, legal proceedings or border measures by Customs. In addition to the routine enforcement mechanisms, campaign-style enforcement has also been frequently used by the Chinese central government in response to crisis situations and mounting foreign pressure. In practice, the multi-pronged enforcement system has failed to stem IPR infringements. While some enforcement mechanisms that have been widely and frequently utilized have little deterrent effect, other enforcement mechanisms that provide a high deterrent effect have also failed to deter due to their underutilization.

For IP rights holders, petitioning a court or applying to an administrative department for enforcement in China can be an ordeal and is very often doomed to fail if it fails to take into account the specifics of the Chinese enforcement system.[598]

### *Administrative Enforcement*

The extraordinarily heavy reliance on administrative enforcement can be regarded as the most distinctive aspect of China's IPR protection. Unlike in many other countries, administrative enforcement by administrative agencies is the method most commonly used in China for IPR protection purposes.[599] Administrative agencies play a much larger role in IPR enforcement than the courts do. Numerous administrative agencies, with overlapping competencies, have general or specialized jurisdiction over IPR administrative protection. Table 10 in the following section 5.4 shows the complexity of IPR administrative enforcement organizations.

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598 Thomas Pattloch, 'Enforcement', in Peter Ganea and Thomas Pattloch (eds.), *Intellectual Property Law in China*, Kluwer Law International, 2005, p. 289.

599 According to Martin K. Dimitrov's comparative study, the ratio of administrative to non-administrative enforcement in China is 106.7:1, whereas in Russia it is 1:2, in Taiwan 1:3.4, in the Czech Republic 1.4:1, in France is 1:3.2, and in the USA 1:585. Martin K. Dimitrov, *Piracy and the State – The Politics of Intellectual Property Rights in China*, Cambridge University Press, 2009, p. 115. Many more studies also highlight the heavy reliance on administrative enforcement in IPR protection in China, especially in trademark protection. For example, 80% of all trademark infringement and unfair competition cases have been dealt with via the following administrative authorities: the Administration of Industry and Commerce, and the Technology and Quality Supervision Bureau. See, for example, Judy Chan and Ross Parsonage, 'Avoid China's Red Tape Evidence Trap', *Managing Intellectual Property*, January 2007, available at http://www.managingip.com/Article/1254172/Avoid-Chinas-red-tape-evidence-trap.html. China's administrative agencies handle 90% of IPR enforcement; Anna-Liisa Jacobsen, 'The New Chinese Dynasty: How the United States and International Intellectual Property Laws are Failing to Protect Consumers and Inventors from Counterfeiting', *Richmond Journal of Global Law & Business*, vol.7, No.1, 2008.

With the exception of patent administrative enforcement, which falls exclusively within the domain of the State Intellectual Property Office (SIPO), IPR administrative enforcement is marked by significant jurisdictional overlap. Six agencies have responsibilities for enforcement in the area of trademarks, while five agencies share the copyright enforcement portfolio at the central level alone. The complex enforcement apparatus, with the poorly defined portfolios, presents serious problems for coordinating the work of the enforcer, as well as for the emergence of effective enforcement. There are numerous options for enforcement that can be delivered by administrative agencies in cases of trademark counterfeiting. Yet instead of making it easier for IPR protection, the existence of multiple enforcers may be the source of many problems. For the reasons discussed below, two radically different outcomes of this situation are the shirking of enforcement responsibilities,[600] and the provision of duplicative, uncoordinated enforcement.[601]

Administrative agencies can take *ex officio* actions at their own initiative, or in response to complaints by rights holders. Generally speaking, they can organize enforcement raids, conduct investigations, order an injunction, confiscate and destroy infringing goods and tools, and impose a fine.[602] Rights holders can institute legal proceedings at the courts if they do not agree with administrative decisions. If the infringement constitutes a crime, administrative agencies will transfer the case to the Public Security Bureau (PSB) for a further criminal investigation. Administrative proceedings have the advantage of being quick and expedient, and lead to high rates of liability being found. Administrative remedies are limited to fines, and at present these fines are too low to deter IPR infringement effectively.[603] Thus, although administrative enforcement has been amply utilized in practice for IPR protection, it fails to deter due to the weakness of the remedies available.

### *Judicial Enforcement*

Judicial enforcement generally refers to actions in court, including civil and criminal law enforcement. Civil law proceedings can be initiated by rights holders wishing to file a lawsuit for infringement at a court. In practice, civil law enforcement often occurs in complex copyright and patent cases, where it is technically difficult to prove either the existence (copyright) or the infringement (patents) of a right. By contrast, administrative enforcement

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600 Sometimes an agency will refuse to enforce, claiming that another agency is better suited to handle a given case.

601 Martin K. Dimitrov, 2009, p. 186.

602 The mandate of each administrative agency in IPR enforcement is different. In contrast to AIC, for example, which is responsible for trademark protection, the SIPO in charge of patent protection has a limited enforcement mandate and limited resources, and thus rarely organizes enforcement raids in response to complaints from rights holders.

603 Where, for instance, fake goods are found, the Quality and Technical Bureau (QTSB) can impose a fine amounted between 50% and three times the value of the products, pursuant to Article 50 of the Product Quality Law.

is more common in trademark cases, where most cases are clear-cut and infringement is easier to prove.

In order to help the regular courts to function better in IP-related cases, China has set up specialized tribunals in intermediate and high courts exclusively to handle civil IPR cases. It should be noted that specialized IPR courts and tribunals are very rare in the world.[604] One reason for this is that more developed countries do not need such specialized tribunals since their ordinary courts can generally function well, including in the area of IPR. In contrast to judges in China's ordinary courts, judges serving on the specialized IPR tribunals in China have very high qualifications and specialized training in law. The creation of IPR tribunals is indicative of the state's resolve to invest scarce resources in an area of the law that is becoming increasingly important,[605] and in ways that allow for partial instead of holistic institutional adjustment of the court system to enhance IPR enforcement.

Criminal enforcement can be initiated in three ways. Firstly, rights holders may directly institute private prosecution proceedings at the courts if they can prove that the infringing party has injured the victim's body or assets and is therefore criminally liable, but the police, i.e. the PSB, or Procuratorate have failed to prosecute the offense.[606] The other two options directly involve the PSB. The PSB can accept transferred cases that were initially handled by administrative authorities and that are found to meet the threshold for criminal liability.[607] As a third option, the PSB itself can also proactively initiate a case.

In theory, due to the highly deterrent effect, criminal enforcement should be considered the most effective method of IPR protection. Indeed China's criminal enforcement does provide severe remedies for IPR infringements, including prison sentences of up to seven years. China has also lowered its criminal liability threshold in response to a WTO complaint lodged by the US.[608] However, China has failed to use its criminal system with sufficient frequency

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604 The comparative study by Martin K. Dimitrov found that only 6% of the 176 WIPO member states had established such courts. Furthermore, these courts had only appellate jurisdiction over IPR cases. China is the only country to have specialized tribunals that accept first-instance civil IPR cases. See Martin K. Dimitrov, *Piracy and the State – The Politics of Intellectual Property Rights in China*, Cambridge University Press, 2009, p. 101.

605 Martin K. Dimitrov, 2009, p. 103.

606 Article 170, Criminal Procedure Law.

607 Article 54, Trademark Law. See also 'Regulation on the Transfer of Suspected Criminal Cases by Administrative Enforcement Agencies', issued on 4 July 2001.

608 For example, the threshold for the crime of counterfeiting a registered trademark, which can result in a fixed-term prison sentence of up to three years, has been reduced from 100,000 to 50,000 Yuan of the illegal business turnover. See Article 1.1 of the 'Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on the Concrete Application of the Law in Handling Criminal Cases of Intellectual Property Infringement', adopted in November 2004.

to create a deterrence.[609] For reasons such as the fact that administrative agencies are loath to initiate a transfer and the PSB often refuses acceptance, transfers of cases from administrative authorities to the PSB for criminal enforcement have not occurred very often, despite what is required by law. In contrast to the administrative enforcement mechanism, which is amply utilized, but fails to deter due to the weakness of the remedies, criminal enforcement that provides strong remedies fails to deter due to underutilization.

### *Customs Enforcement*

The Chinese Customs Service provides border protection of IPR. This serves two functions: first, if counterfeit goods are produced in China for export to another country, Customs can stop the goods from being exported abroad; second, if fake goods are imported into China from another country, Customs can prevent the importation of the goods into the Chinese domestic market. Rights holders can obtain redress through Customs enforcement in two ways. The first option is to make a request to Customs to detain a shipment of infringing goods. In the second option Customs engages in proactive *ex officio* actions to protect IPR goods that have already been recorded in the Customs database. If Customs discover goods suspected of infringing a recorded right, they may give the rights holder the option of making a request to detain the goods. If the rights holder decides to make the request, the goods will be detained upon payment of a bond or issuance of a bank guarantee.

Border protection of IPR is important since cross-border trade in IPR-infringing goods is a serious business. In 2007, Chinese Customs prevented the importation and exportation of more than 334 million items worth 439 million yuan (US$ 64 million), which was 83% higher in amount and 116% in value than in 2006.[610] What is unusual is that 99.8% of the captured goods were destined for export.[611] While most countries use Customs to prevent importation of IPR-infringing goods in order to protect their domestic market, China uses Customs chiefly to protect *other* countries by stopping the exportation of counterfeits.[612] This demonstrates that China's allocation of Customs resources to IPR protection is mainly in response to foreign pressure, rather than as a result of domestic demands.

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609 Omario Kanji, 'Paper Dragon: Inadequate Protection of Intellectual Property Rights in China', 27 Michigan Journal of International Law, 2006; Mark Liang, 'A Three-Pronged Approach: How the United States Can Use WTO Disclosure Requirements to Curb Intellectual Property Infringement in China', Chicago Journal of International Law, Summer 2010; Martin K. Dimitrov, 2009, p. 146; Frank Lin, 'Piracy in China: Identifying the Problem and Implementing Solutions', *Currents: International Trade Law Journal*, vol. 14, 2005.

610 China Custom IPR Protection Report 2007, issued by the General Custom Administration in April 2008.

611 China Custom IPR Protection Report 2007, issued by the General Custom Administration in April 2008.

612 Martin K. Dimitrov, 2009, p. 79.

*Campaign-style Enforcement*

When facing with great international pressure and the risk of trade wars triggered by other WTO member countries' dissatisfaction, the Chinese government's habitual reaction is to launch periodic anti-counterfeiting and anti-piracy campaigns and to issue various specific rules to show the world that it is continuing to make progress in IPR protection.[613] However, foreign pressure can be regarded as only a partial reason for those campaigns. Campaign-style enforcement is also China's habitual reaction to a need for rapid resolution of a major problem in many domestic domains. In the field of IPR enforcement, campaigns typically feature market sweeps during a short period of concentrated enforcement. The SIPO, for instance, organized the 'Thunder' and 'Sky Net' nationwide patent enforcement campaigns, which were intensively conducted between 26 April and 26 May 2010 by IPOs and with the cooperation of other IPR-mandated administrative agencies at all local levels.[614] Enforcement campaigns always involve the collaboration of at least two, and sometimes many more, agencies. Sending three thousand enforcement personnel to a village of twenty thousand is an example of campaign-style enforcement. In China's Annual Action Plans on IPR Protection, which started being issued in 2006, 'carrying out special IPR enforcement campaigns',[615] rather than 'enhancing routine enforcement', has consistently been given first priority in efforts to improve IPR enforcement.[616] The strong reliance on campaign-style enforcement reveals the basic problem facing the Chinese government in respect of enforcement: routine enforcement raids are ineffective, which means relatively small-scale problems eventually require the unleashing of enforcement campaigns.[617] Even worse, these campaigns are not necessarily effective at resolving the problem:[618] counterfeiting operations merely move to the next village or a new town, and the fake goods continue to be churned out until the next crisis, in a predictable cyclical pattern, results in the next campaign.[619] In the end, campaign-style enforcement represents a waste of administrative efforts and delivers high volumes of low-quality enforcement. It cracks down on rampant counterfeits and piracy in the short term, but lacks a long-term deterrent effect, and thus cannot be a proper and adequate response to IPR enforcement problems caused by institutional obstacles.

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613 Paul Torremans, Hailing Shan, Johan Erauw (eds.), *Intellectual Property and TRIPS Compliance in China*, Edward Elgar Publishing Limited, 2007, p. 5.

614 Action 'Thunder' targeted patent infringement and counterfeiting, while Action 'Sky Net' mainly targeted patent passing-off. 'Special Action Program of IPR Enforcement 2010', issued by the SIPO.

615 In Chinese, it is '*kaizhan zhishi chanquan zhuangxiang yudong*'.

616 China's Action Plans on IPR Protection (*zhongguo baohu zhishi chanquan xingdong jihua*) of 2006, 2007, 2008, 2009, 2010 and 2011. The Action Plans have been compiled by the National IPR Protection Working Group Office, in conjunction with 28 other relevant departments, including the Publicity Department of the CPC Central Committee, the Ministry of Foreign Affairs, the National Development and Reform Commission, and the SIPO.

617 Martin K. Dimitrov, *Piracy and the State – The Politics of Intellectual Property Rights in China*, Cambridge University Press, 2009, pp. 4-5.

618 Paul Torremans, Hailing Shan, Johan Erauw (eds.), 2007, p. 5.

619 Martin K. Dimitrov, 2009, p. 5.

## 5.4 TRANSPARENCY IN ENHANCING IPR ENFORCEMENT

As discussed in Chapter III, there is a general lack of transparency in the Chinese legislative regime, mainly due to the interwoven law-making and the existence of excessive numbers of informal legal sources. The transparency problem undoubtedly also exists in the area of intellectual property protection. This section examines the transparency situation and how it affects IPR enforcement in China.

Since the vague enforcement provisions in TRIPS have attracted criticism for their limited ability to induce compliance, some people have proposed using the transparency requirement in TRIPS as an alternative means of achieving better compliance. Article 63.1 of the TRIPS Agreement imposes a transparency obligation on member countries. It states that:

> Laws and regulations, and final judicial decisions and administrative rulings of general application, made effective by a Member pertaining to the subject matter of this Agreement (the availability, scope, acquisition, enforcement and prevention of the abuse of intellectual property rights) shall be published, or where such publication is not practicable made publicly available, in a national language, in such as manner as to enable governments and right holders to become acquainted with them.

Unlike Articles 41 and 61, Article 63.1 does not just state broad principles, but enunciates a more exacting rule. A 'publication' obligation is easier to measure than the obligation of 'effective enforcement'. Moreover, countries are obliged to publish not only laws and regulations, but also judicial and administrative decisions pertaining to IPR.

With regard to the publication of laws and regulations, the Ministry of Commerce, for example, started publishing its own gazette after the accession negotiations of 1993, while also sporadically publishing trade-related laws and regulations adopted. This gazette does not include relevant provincial or local ordinances or normative documents. Instead it contains only laws and regulations published at the national level. Some local governments have also established their own websites to make local regulations publicly accessible. However, disclosure is far from complete and stable. Only parts of local regulations are published, and then only selectively. Indeed, the government's legal gazette often fails to provide notice of changes in administrative rules and regulations, and the public has no steady and

direct access to legal databases.[620] Despite its commitments in the Accession Protocol,[621] China has not designated or established a single journal dedicated to the publication of all laws, regulations and other measures at both national and local levels. The appropriate authorities consequently have to continue referring to several different sources, such as newspapers, journals, and also ministry websites, often without any translation being available. The generally limited extent of publication also applies in respect of IP-related laws and regulations.

As far as publication of judicial and administrative decisions is concerned, there is no comprehensive and searchable system for Chinese judicial decisions. The Supreme People's Court publishes a gazette of judicial decisions.[622] However, this is highly edited and contains only a select proportion of all lower court decisions.[623] The only opinions published are those that the Supreme People's Court deems relevant, and there is no precise standard for determining which opinions are deemed relevant for publication.[624] Although selected cases are published on academic websites or in official court journals,[625] the same problem arises in that publication is not regular and there is no precise standard for the selection. Most of the court decisions published are those issued by the SPC, the High Court at provincial level or the intermediate courts in major cities. Basic courts' decisions, which are the major component of judicial rulings in China, are rarely published, and even if such decisions are deemed appropriate for publication, they are often revised or edited to make the opinions 'exemplary models' for other courts.[626] China's current disclosure practices therefore fail to meet the requirements of Article 63.1.

Some specific efforts have been made to enhance the publication of judicial decision pertaining to IPR. Since 10 March 2006, the 'China IPR judgments and Decisions' website,[627]

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620 Wei Shi, 2008.

621 Accession Protocol, I, 2, C, 2, which requires that 'China shall establish or designate an official journal dedicated to the publication of all those laws, regulations and other measure pertaining to or affecting trade in goods, services, TRIPS or the control of foreign exchange and, after publication of its laws, regulations or other measures in such journal, shall provide a reasonable period for comment to the appropriate authorities before such measures are implemented'.

622 The Supreme People's Court maintains a website that posts cases published in the Gazette. This is available at http://www.court.gov.cn.

623 Thomas E. Volper, TRIPS Enforcement in China: A Case for Judicial Transparency', 33 *Brooklyn Journal of International Law*, 2007.

624 Brent T. Yonehara, 'Enter the Dragon: China's WTO Accession, Film Piracy and Prospects for the Enforcement of Copyright Laws', *UCLA Entertainment Law Review*, No. 9, 389, Spring 2002.

625 Judicial cases, for instance, are published in http://vip.chinalawinfo.com/ and http://www.lawyee.net/, both of which are operated by Peking University, and on the official website of the High Court of Guangdong Province http://www.gdcourts.gov.cn/alxc/index.jsp.

626 Karen Halverson, 'China's WTO Accession: Economic, Legal and Political Implications, 27, *British Columbia International & Comparative Law Review*, 2004; Brent T. Yonehara, 2002.

627 http://ipr.chinacourt.org/, (*zhishi chanquan weishu caipan wang*).

established under the Chinese Court Net (*Zhongguo Fayuan Wang*),[628] has published all IPR-related judicial decisions made by courts at all levels in China. In the four years to 2010, a total of 41696 judgments were posted on the website. However, according to the Supreme People's Court's annual report, the number of first-instance IPR cases judged in China was 23518 in 2008,[629] 30509 in 2009,[630] and 41718 in 2010.[631] Obviously, therefore, only a small portion of judgments are selected for publication on the website.

The problem of selective publication can also be found in some websites established by local courts. On 1 November 2003, for example, the High People's Court in Beijing announced that, from that date, all intellectual property judgments delivered by courts in Beijing would be posted on its website, Beijing Court Net (*Beijing Fayuan Wang*).[632] The announcement emphasized that the Beijing courts had taken the unprecedented step in the Chinese legal system of publishing every intellectual property judgment. By June 2006, 497 judgments had been posted on the website. However, China's SIPO reported that the First Intermediate People's Court of Beijing and the High People's Court of Beijing had ruled on a total of 592 and 485 patent judicial review cases in 2004 and 2005 respectively.[633] These 1077 cases alone outnumber all the judgments posted on the website. Although the reason and criteria for the selective publication are unknown, the posted cases are likely to have been carefully selected to show these courts in a favorable light.

Without transparency, IPR holders will continue to suffer as a result of the lack of certainty, the incongruity between laws, and unexpected political interventions. Non-transparency of judicial decisions makes it difficult for parties to perform effective evaluations of and predictions on their litigation. China's IPR enforcement has been criticized for its failure to provide deterrence. Certainty of punishment, as opposed to severity of punishment, is more important and most needed in China for effective deterrence. Transparency plays an essential role in ensuring certainty of IPR enforcement. If all IPR-related judicial and administrative decisions are published, the certainty and predictability of IPR enforcement in China will be greatly enhanced. Litigants can then develop expectations of what their legal rights are and adjust their behavior accordingly, including taking preventive measures to protect their IPR in situations where courts are known to disfavor strong IPR protection and relying more on adjudication in situations where courts are known to favor strong IPR protection.[634] Judges and administrative officials will also have a more complete supply of

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628 http://chinacourt.org/.

629 http://www.ipr.gov.cn/zfxxarticle/govinfo/govtjxx/200903/271206_1.html.

630 'Judicial Protection of Intellectual Property Rights in Chinese Courts in 2009', Supreme People's Court.

631 'Judicial Protection of Intellectual Property Rights in Chinese Courts in 2010', Supreme People's Court

632 Zhang Xuecong, 'Intellectual Property Judgments Can Be Searched on the Net', *Zhongguo Fayuan Wang*, (Chinese Court Net), 1 November 2003, available at www.chinacourt.org.

633 State Intellectual Property Office, Annual Report 2004 and Annual Report 2005, available at www.sipo.gov.cn.

634 Mark Liang, 2010.

precedents from other jurisdictions. Publication of court decisions will increase consistency in the application of law. As a result, IPR cases can be expected to be decided with greater competence and increased uniformity.

More transparency will also result in increased scrutiny of judicial and administrative rulings. The court's reasoning in the adjudication instrument is too simple and vague, lacking explanation of the basis for its judgment.[635] As illustrated in the case study discussed in section 5.5.2, the court rejected the method proposed by the plaintiff for calculating the compensation and made its own judgment of 300,000 yuan as the remedy for the plaintiff, without specifying how or on what basis the sum had been calculated. Lack of reasoning in a court's ruling makes the judgment seem subjective and open-ended, thus creating difficulties in convincing the parties in the present case and in unifying the judging standards for similar cases in future. Being aware that their decisions are publicly available and subject to review from higher courts, the central government and even other WTO members, judges and administrative panels may feel pressured into making more deliberate rulings. The judiciary, particularly the lower courts, will be more inclined than at present, when their decisions are rarely disclosed and scrutinized, to adjudicate their cases in full compliance with IPR laws and regulations.[636]

Non-transparency is also one of the main contributors to the unpredictable and capricious administrative enforcement of IPR. The difficulty in transferring cases from administrative agencies to PSBs for criminal enforcement, for example, is partially attributed to low transparency in administrative IPR enforcement proceedings. As discussed in the following sections, administrative agencies are loath to initiate a transfer, in part because transfers act as an indirect instrument of bureaucratic accountability by allowing other government agencies to receive information. If transparency in general could be enhanced in administrative enforcement, administrative agencies would have less reason to refuse a transfer. At the same time, enhancing the transparency of public and inter-bureaucratic supervision would deter administrative agencies from retaining cases that qualify for criminal enforcement.

635 Investigation Team in the High Court of Guangdong Province, 'New Problems in Judicial Protection of Intellectual Property Rights after the WTO Accession – Investigation on IPR Judicial Protection in Guangdong Province', *Law Application*, No. 231, 2005.

636 Mark Liang, 2010.

## 5.5 FRAGMENTATION PROBLEM IN IPR ADMINISTRATIVE ENFORCEMENT

Chapter IV examines the deficiency of uniform administration in the application of laws in China and the consequent problem of market fragmentation. The fragmentation problem, which exists not only in the economic area, but also widely in the administrative system, is attributed mainly to local government's abuse of its administrative power and to protection measures, as well as to the central government's difficulty in ensuring uniform administration. This section discusses how the fragmentation problem hinders IPR enforcement conducted by administrative organs at local levels.

The tension in the central-local hierarchy, which is interwoven with the underdeveloped administrative and legal system, takes the fragmentation problem far beyond the scope of 'market' or the free movement of products. In China's political and economic systems, and in many other fields, there is a long-term branches-versus-areas (*tiaotiao-kuaikuai*) administration system, which is referred to by Lieberthal as fragmented authoritarianism.[637] Under this system, the national administrative authority is vertically segmented by branches and sectors such as industrial ministries (*tiaotiao*), and horizontally segmented by regions such as provinces (*kuaikuai*).[638] The vertical lines of authority block proper cooperation between different departments, while the horizontal lines of authority block proper cooperation between different local regions. IPR enforcement is contingent on a high degree of cooperation between different regions. One counterfeiting activity may take place in various regions, including manufacture of generic products and counterfeited trademarks, as well as packing, storage and distribution. Cooperation between different institutions is equally important since various administrative agencies, judicial organs and public security organs may concurrently get involved in a single IPR infringement case. The fragmentation

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637 Fragmented authoritarianism model argues that authority below the very peak of the Chinese political system is fragmented and disjointed. The fragmentation is structurally based and has been enhanced by reform policies regarding procedures. Kenneth G. Liberthal, "Introduction: The 'Fragmented Authoritarianism' Model and Its Limitations", in Kenneth G. Lieberthal and David Lampton (ed,) *Bureaucracy, Politics, and Decision-Making in Post-Mao China*, California University Press, 1992.

638 For more discussions on *tiaotiao-kuaikuai* administration in China, see Paul E. Schroeder, 'Territorial Actors as Competitors for Power: The Case of Hubei and Wuhan', in Kenneth G. Lieberthal and David Lampton (ed,) *Bureaucracy, Politics, and Decision-Making in Post-Mao China*, California University Press, 1992.Stig Thogersen and Soren Clausen, 'New Reflections in the Mirror: Local Chinese Gazetteers (Difangzhi) in the 1980s', *The Australian Journal of Chinese Affairs*, No. 27, 1992; Jorgen Delman, 'Cool Thinking? The State Role in Shaping China's Dairy Sector and Its Knowledge System', *China Information*, The Documentation and Research Centre for Modern China, Sinological Institute, Leiden University, vol. 17, No. 2, 2003. See Chinese literature: Shutang Gu, *Discussions on Reform of Chinese Planning System*, China Social Science Press, 1987; Jie Wu, *Reform of Chinese Government and Institutions*, China National School of Administration Press, 1998; Shangqing Sun, *New Economic Problems*, China Development Press, 1996; Congbing Wu, 'Reduce TiaoKuai Fragmentation, Establishing Assistance Institutions – Improvement on the Reform of China's Environmental Institutions', *Public Administration and Law*, issue 4, 2004.

problem in China, no matter whether it is bureaucratic or economic, horizontal or vertical, makes it an inhospitable environment for IPR enforcement to take root. IPR enforcement provides a perfect window on the fragmentation problem in policy-making, administration and enforcement in contemporary China.

## 5.5.1 Problems of Administrative Enforcement Mechanism – Vertical Fragmentation

### *5.5.1.1 Fragmented Institutional Structure*

The IPR administrative enforcement system consists of numerous enforcement agencies with concurrent and sometime overlapping jurisdictions. IPR enforcement is decentralized among a number of different administrative entities because the Chinese administrative system is designed to cope with a socialist economy divided into vertical sectors (*tiaotiao*). At the central level, the SIPO is in charge of patents, while the State Trademark Office under the State Administration on Industry and Commerce (SAIC) is the competent authority for trademarks, and the National Copyright Administration associated with the National Press and Publications Administration is the competent authority for copyright. These IPR apparatus are not only discrete vertical units themselves, but also belong to distinct bureaucratic clusters, *xitong*, across which member officials have traditionally had very little contact. Patents fall under the science and technology *xitong*, while copyright falls under the propaganda and culture *xitong*, and trademarks fall under the finance and economic *xitong*. The table below illustrates the institutional structure of IPR protection at the central and local levels.

**Table 10: Competent Administrative Authorities for IPR Administrative Enforcement**

| IPR Types | Competent Authorities at Central and Local Levels | Jurisdiction |
|---|---|---|
| Patent | State Intellectual Property Office (SIPO)[639] | Enforcement in event of patent infringement, patent counterfeiting and patent passing-off;[640] Application of patent approval, re-examination and invalidation |
| | *Intellectual Property Bureau (IPB) at local levels* | |
| Trademark | State Administration for Industry and Commerce (SAIC)[641] | General jurisdiction: trademark counterfeiting |
| | *Administration of Industry and Commerce (AIC) at local levels* | |
| | State Administration of Quality Supervision, Inspection and Quarantine (AQSIQ) | General jurisdiction: trademark counterfeiting |
| | *Quality and Technical Supervision Bureau (QTSB) at local levels* | |
| | Ministry of Health (MOH) | Specialized jurisdiction: counterfeiting in food, pharmaceuticals and cosmetics |
| | *Public Health Bureau (PHB) at local levels* | |
| | State Food and Drug Administration (SFDA) | Specialized jurisdiction: counterfeiting in food, pharmaceuticals and cosmetics |
| | Food and Drug Administration (FDA) at local levels | |
| | Ministry of Agriculture (MOA) | Specialized jurisdiction: counterfeit agricultural inputs |
| | *Agriculture Bureau at local levels* | |

639 The SIPO is the only administrative agency with jurisdiction over patent matters in China today. Contrary to what the name of the organization indicates, the SIPO is not responsible for all subtypes of IPR, but only for patent issues and for representing China in international patent and trademark meetings.

640 Under Chinese Patent Law, an infringement (*qinquan*) is an act of using, making, or selling a patented invention without authorization (Patent Law, Article 57). Passing off (*maochong*) an unpatented product as a patented invention refers to activities such as printing a likeness of the name of the patent holder and patent number and affixing them to a product similar to the product embodying the invention for which the patent has been granted. Patent counterfeiting (*jiamao*) involves counterfeiting the patent certificate or other patent document belonging to the legitimate holder of the patent. In practice, the SIPO has concerted its enforcement activities in areas where it has exclusive jurisdiction (patent counterfeiting and patent passing-off) and has de-emphasized enforcement in the case of patent infringements, where the courts also have jurisdiction and have emerged as the dominant providers of enforcement.

641 As a main enforcer of trademark protection, the SAIC participates in anti-counterfeiting on three grounds: first, counterfeiting constitutes unfair competition; second, counterfeiting may impact consumer health and safety; finally, counterfeits are often sold through false and misleading advertisement. Thus, a total of four departments within the SAIC have overlapping mandates over counterfeiting: the Fair Trade Department, the Consumer Protection Department, the Advertisement Supervision Department, and the Enforcement Team.

| | | |
|---|---|---|
| | State Tobacco Monopoly Administration (STMA) | Specialized jurisdiction: counterfeit tobacco products |
| | Tobacco Monopoly Administration (TMA) at local levels | |
| Copyright | General Administration of Press and Publications (GAPP) | Jurisdiction on copyright matters mainly at central and provincial levels[642] |
| | *Press and Publications Bureau (PPB) at local levels* | |
| | National Copyright Administration (NCA) | Functions as a department of the GAPP with lower bureaucratic standing[643] |
| | *Copyright Bureau at local levels* | |
| | Ministry of Culture (MOC) | Jurisdiction over copyright matters at county level and below[644] |
| | Culture Bureau at local levels | |
| | State Administration of Radio, Film and Television (SARFT) | |
| | Office of National Anti-Pornography and Anti-Piracy Working Committee (NAPWC) | |

It should be noted that the SIPO was established in 1998 with the deliberate aim of conforming to the traditional notion of 'intellectual property' and institutionalizing this tradition into a concrete bureaucratic agency.[645] In theory, the SIPO should manage and coordinate the activities of the patent, copyright and trademark bureaucracies.[646] In reality, however, it continues to exercise patent-related functions like the former Patent Bureau.[647] As an organization it is largely adrift and often disconnected from the actual institutional and political arena in which non-patent-related IPR protection and enforcement in China take place.[648]

642 At the central level, the GAPP and NCA are actually one organization with two names (*yige jigou liangkuai paizi)*. At the provincial level, there are normally only the PPBs, which are also in charge of copyright administration.

643 Copyright bureaus are often subordinated to and combined within the PPB at provincial levels.

644 At county level, the functions of the Copyright Bureau and the Press and Publications Bureau are often subordinated to and combined within the Culture Bureau. The bureaucratic arrangements with regard to these three administrative agencies vary from one region to another.

645 Andrew Mertha, *The Politics of Piracy – Intellectual Property in Contemporary China*, Cornell University Press, 2005.

646 Andrew Mertha, 2005.

647 Xuezhong Zhu and Jing Huang, 'Integration of Administrative Institutions of Intellectual Property Rights', *Science Technology and Law (Keji he Falv)*, issue 3, 2004.

648 Andrew Mertha, 2005.

The actual IPR institutional structure is far more intricate than illustrated in the above table, if local agencies are taken into account. At the local level, the IPR agencies are slightly different from those at the central level and vary from region to region. For copyright administration at the provincial level, for example, the Provincial Culture Bureau and the Provincial Press and Publication Administration are the competent authorities. Under the provincial level, the competent authority is the Culture Bureau, which is in charge of the 'cultural market', including movies, live performances, books and periodicals, audiovisual products, crafts, fine arts and so on. The local radio and television bureaus can also take part in activities against piracy on audiovisual products. In some regions, the cultural bureaus, press and publication administration, and the radio and television bureaus have been merged into one institution, while in others they remain separate. The patent administration agencies are as multifarious as copyright authorities at the local level, and titled as intellectual property bureaus, patent bureaus or science and technology bureaus. In contrast to the fragmented administrative system of IPR in China, a uniform IPR protection mechanism has been universally adopted in more than 180 of the 196 countries and regions by combining the administration of patents and trademarks into a single institution: an intellectual property rights agency or a patent and trademark agency. Of these 180 countries, a total of 74, including the US, UK and Russia, have established a uniform IPR mechanism concurrently regulating patents, trademarks and copyright.[649]

Instead of making it easier to protect IPR, the abundance of choice in terms of enforcement agencies may be the source of many problems. It can lead to two radically different outcomes: one is the shirking of enforcement responsibilities by claiming that another agency is better suited to handle a given case; and the other is the provision of duplicative, uncoordinated enforcement.[650] Two specific aspects demonstrate how the presence of multiple enforcers, with poorly defined enforcement mandates, may undermine the effective IPR enforcement.

Firstly, overlapping jurisdiction on IPR infringement has exacerbated bureaucratic rivalries among various parallel government entities, thus creating competition in political interests that discourages coordination and cooperation.[651] According to Articles 53-55 of the Trademark Law, the Administration of Industry and Commerce (AIC) has the sole responsibility for trademark enforcement at all levels. In reality, however, the Quality Technical Supervision Bureau (QTSB) is authorized to bring enforcement actions against

649 Shan Xiaoguang and Wang Zhenyu, 'Institutions of IP Administration in Various Countries and the Inspirations on China', Tongji University Journal Social Science Section, vol. 18, No. 3, June 2007; Zhu Xuezhong and Huang Jing, 2004.

650 Martin K. Dimitrov, 2009, p. 186.

651 USTR Keeps China under 'Section 306' Monitoring – Except from 2002 Intellectual Property Protection Report, State Dept. Press Release and Documents, 1 May 2002, available at 2002 WL 25970050; Daniel C.K. Chow, 'Enforcement against Counterfeiting in the People's Republic of China', 20 *Northwestern Journal of International Law and Business*, 2000; Sandy Meng-Shan Liu, 'After WTO Accession: China's Dilemma with the Trafficking of Fakes', *The Trademark Reporter*, September-October 2003.

manufacturers or sellers of counterfeit products inferior in quality and fakes that defraud or harm the public under the Product Quality Law.[652] Insofar as counterfeit merchandise is of inferior quality relative to its legal counterparts, and insofar as the unknowing purchase of such counterfeits harms the consumer, the QTSB can reasonably target the manufacture and sale of such offending merchandise.[653] In addition to being responsible for investigating counterfeit products in the name of quality supervision, the QTSB plays a substantial role in the 'crackdown on fakes' (*da jia*) campaign against faked products. In the local regulation on 'crackdown on fakes' in Guangdong province, for instance, Article 5 provides that both the QTSB and AIC above county level shall be in charge of 'cracking down on fakes' within each jurisdiction.[654] Products covered by this regulation include products with counterfeited trademarks, pirated copyright and faked patents, as well as unqualified products.[655] In the name of 'crackdown on fakes', the local QTSB and AIC are *de facto* empowered to bring enforcement actions in protection of trademarks, patents and copyright.

Under the overlapping jurisdiction, the rivalry for power between the various authorities that discourages cooperation is partly attributable to the longstanding bureaucratic fragmentation between different industries under the *tiaotiao* administration model. Since 1994, the QTSB has liberally interpreted its role to include directly and aggressively combating the production and sale of counterfeit goods, thus intruding on what had formerly been the anti-counterfeiting responsibilities of the AIC.[656] This has led to a sometimes intense inter-bureaucratic tension.[657] The QTSB is continuing to expand its enforcement actions against counterfeiting in an effort to increase its capacities and power vis-à-vis its bureaucratic

652 Sandy Meng-Shan Liu, 2003. The Product Quality Law was issued in February 1993 and revised in July 2000. Article 8 of the Product Quality Law states that the QTSB at the levels above county is in charge of the supervision and control of product quality. Article 53 states that where a producer or a seller forges the origin of a product or falsely uses another producer's name and address, or forges or falsely uses authentication marks or other quality marks, the producer or seller shall be ordered to make public rectification, the products that are unlawfully sold or produced shall be confiscated, and the unlawful earnings shall be confiscated; a fine which is less than the value of those unlawfully produced or sold products shall be imposed concurrently; in serious cases, the producer or seller's business license shall be revoked.

653 Andrew Mertha, 2005.

654 Regulations on Crackdown Counterfeited, Faked and Inferior-Quality Products (*jiamao weilie*) of Guangdong Province, issued in September 1999. Similar provisions can also be found in other regions' local regulations, for example the Regulations on Prohibiting the Manufacture and Sale of Counterfeited, Faked and Inferior-Quality Products (*jiamao weilie*) of Wuhan City, issued in January 1995 and revised in November 2001, Article 3 states that QTSB and AIC are the competent authority for 'crackdown fakes' required under this regulation; Article 6 contains the same definition on 'fakes' as the regulation of Guangdong Province.

655 Regulations on Crackdown Counterfeited, Faked and Inferior-Quality Products (*jiamao weilie*) of Guangdong Province, issued in September 1999.

656 Andrew Mertha, 2005.

657 Andrew Mertha, 2005.

competitors and thus corner the market in IPR enforcement.[658] The incentive behind the QTSB is summarized by one experienced observer as, 'To be very clear, the competition is over money'.[659] Issuing fines, collecting fees, and obtaining side payments from trademark right-holding 'clients' provide these enforcement agencies with extra-budgetary revenue that would be impossible to secure through normal budgetary allocation processes.[660] Very often, the confiscated counterfeited goods, which are normally of fair quality, are handed out to QTSB employees as a bonus or welfare.[661]

For both QTSB and AIC, 'having authority' to combat counterfeiting means larger budgets, and more staffing, power and prestige.[662] The central government previously tried to institutionalize AIC-QTSB competition and to give it an official endorsement from the State Council. This effort, however, failed because of AIC-QTSB deadlock on the issue of which one should take the leading role in joint action.[663]

Although increased competition between these two authorities may enhance IPR protection from a certain perspective, it may at the same time transform the nature of trademark enforcement work if the interest in striking down counterfeited products conflicts with the interest in expanding power and income. Given the fierce competition between the AIC and QTSB, the latter interest may be given priority if it is associated with greater rewards for the authorities. If an IPR-infringing enterprise provides the authorities with a reasonably steady flow of income, it is very likely that the authorities will not only refrain from closing down the factory, but may also actively seek to 'protect their investment', particularly given the ceiling of 10,000 yuan for counterfeit-related fines.[664] Moreover, a single agency is responsible for both licensing and enforcement. Sometimes, properly licensed firms engage in illegal behavior, such as counterfeiting piracy. Pursuing these firms with the full force of the law may drive them out of business, thus risking potential harm to the economic well-being of the locality; it may also eliminate the lucrative fees that the agencies collect from their licensing activities. In such situations, particularly if they are under pressure to expand their power and income, agencies may refrain from enforcing in order to protect the guilty firm. Thus, overlapping jurisdictions and 'competition for power' encourage local protectionism of IPR infringers. Another result is the shirking of enforcement responsibilities. If an agency is unwilling to enforce, it may claim that another agency is better suited for the enforcement. In some cases, agencies may enforce the request of the rights holders,

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658 Andrew Mertha, 2005; Xuezhong Zhu and Jing Huang, 2004.

659 Andrew Mertha, 2005.

660 Andrew Mertha, 2005; Daniel Chow, 'Anti-counterfeiting Strategies', 2010; Mark Liang, 2010.

661 Interview with the QTSB official in Guangdong province, 7 November 2005.

662 Andrew Mertha, 2005.

663 Andrew Mertha, 2005.

664 The ceiling for counterfeit-related fines may vary from region to region. The amount of 10,000 yuan is the standard in Guangdong province according to the Regulations on the Crackdown on Counterfeited, Faked and Inferior-Quality Products (*jiamao weilie*) of Guangdong Province, see footnote 622.

but their enforcement will be selective, focusing on 'easy' cases, such as checking whether stores sell counterfeits, rather than on the hard task of detecting and closing down the enterprises that actually produce the counterfeits.

Jurisdictional overlap among various agencies also makes for low efficiency and low-quality enforcement. Low efficiency is a product of uncoordinated enforcement. Most of the time the agencies work against one another instead of cooperating on enforcement. This leads to duplication and a waste of administrative effort if, for example, the same stores are repeatedly checked, whereas others are repeatedly ignored. Another example is that when dealing with patent infringement disputes that also involve a trademark infringement, the local patent departments tend only to pursue the patent infringement liability.[665] Cases relating to both trademark and copyright infringements are dealt with exclusively, rather than in a coordinated manner, either by the AIC or by the copyright authority. The uncoordinated enforcement contributes to the heavy reliance on periodic 'concentrated enforcement' campaigns organized by the central government, when agencies at all levels of government from the center down to the county must register some enforcement. If one agency's force is weakened because of authority fragmentation, combined actions become an inevitable solution for the sweeping IPR infringements. However, the quality of these temporary joint enforcement actions is low. The joint actions between authorities can only be provisional, in the form of waves, rather than consistent and sustained enforcement. Once the campaign is over, the *status quo ante* often returns until the start of the next campaign.[666]

### *5.5.1.2 Difficulties in Transferring Cases from Administrative Authorities to Criminal Authorities*

Criminal enforcement of IPR is particularly important in China since administrative remedies are inadequate as a deterrent, and are perceived by IPR infringers simply as a cost of doing business.[667] After the WTO accession, a complaint was filed against China with regard to its rarely used criminal procedures for IPR protection.[668] China subsequently lowered the threshold for IPR crimes (from 100,000 yuan to 50,000 yuan of the illegal business turnover in the case of counterfeiting registered trademarks, for instance) and clarified the rules on how to calculate 'illegal business turnover'.[669] In practice, however, the major obstacle to

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665 Xuezhong Zhu and Jing Huang, 2004.

666 Counterfeiting operations are merely moved to the next village or the next town, and the fakes continue to be churned out until the next crisis, in a predictable cyclical pattern, results in the next campaign. Martin K. Dimitrov, 2009, p. 5; Andrew Mertha, 2005, p. 144.

667 Sandy Meng-Shang Liu, 2003.

668 The WTO complaint lodged by the US in the case of *China – Measures affecting the Protection and Enforcement of Intellectual Property Rights*, WTO DS362, 2007.

669 Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on the Concrete Application of the Law in Handling Criminal Cases of Intellectual Property Infringement, adopted in November 2004.

criminal enforcement in IPR remains the fact that so few cases are placed on the docket. In 2005, for example, the AICs at all levels in the entire country handled 6332 cases of trademark counterfeiting in which the value of infringement was over 50,000 yuan,[670] thus meeting the criminal liability threshold. In the same year, however, the AICs at all levels transferred only 236 cases to the PSB.[671] This means that only 3.7% of the cases that met the threshold for transfer were actually transferred to the criminal authorities.

Most often a case reaches the police through an administrative agency, which must be willing to consider transferring the matter to the police in the first place if the illegal business turnover exceeds the designated criminal threshold.[672] The police must then decide to accept the case and, thereafter, to transfer it to the Procuratorate, which in turn must decide whether to pursue the matter by arresting the suspect and bringing the case to court. Although many of the cases handled by administrative agencies are indeed serious enough to merit being transferred to the police for criminal prosecution, negative incentives at each stage of the criminal process limit the number of cases that are actually prosecuted and ultimately reach the courts.[673] Difficulties that exist at the stage of transferring cases from administrative agencies to the PSB are discussed in detail below.

There are three main obstacles to transferring cases from administrative agencies to the PSB. The first one relates to the difficulty in calculating the illegal business turnover, which is essential for deciding whether there is criminal liability. Criminal liability is based upon a bright-line standard measured by the amount of sales in counterfeited or pirated goods. The value of the infringement depends on the price of the infringing products sold or, if the products have not been sold, the marked price or the average actual sale price.[674] If there is no marked price, the price is calculated in line with the median market price of the infringing products.[675] In practice, it can be extremely difficult for administrative agencies, relying on their own means and measures, to identify the marked price or actual average

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670 50,000-100,000 yuan: 5173 cases; 100,000-300,000 yuan: 809 cases; 300,000-1,000,000 yuan: 249 cases; 1,000,000 yuan and more: 101 cases. See 'Basic Situation of Trademark Counterfeiting Investigations in 2005' (*2005 nian quanguo chachu shangbiao weifa anjian jiben qingkuang*), 27 April 2006.

671 109 cases were transferred by the AIC in Zhejiang province, 19 cases by Beijing, 19 cases by Fujian province, 17 cases by Guangdong province, 12 by Jiangsu province, 11 cases by Shanghai, and 49 cases by the AICs in the rest of the country. See 'Basic Situation of Trademark Counterfeiting Investigations in 2005' (*2005 nian quanguo chachu shangbiao weifa anjian jiben qingkuang*), 27 April 2006.

672 Provisions on the Transfer of Suspectable Criminal Cases by Administrative Organs for Law Enforcement, issued by the State Council in July 2001, Article 3.

673 Martin K. Dimitrov, 2009, p. 146.

674 Article 12, Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on the Concrete Application of the Law in Handling Criminal Cases of Intellectual Property Infringement, adopted in November 2004.

675 Article 12, Interpretation of the Supreme People's Court and the Supreme People's Procuratorate on the Concrete Application of the Law in Handling Criminal Cases of Intellectual Property Infringement, adopted in November 2004.

sale price.[676] Administrative agencies will then tend to adopt the 'median price' of infringing products in the market, which is normally referred to as the price of genuine products and is easier for administrative agencies to identify.[677] However, in the same situation, the PSB will tend to calculate the price based on the value of the faked products, which could be much lower than the price of genuine ones, thus reducing the value of infringing products below the threshold for criminal investigation.[678] The different calculation method applied may mean the PSB returns the case to the administrative agencies.[679] Administrative agencies will regard this return of the case as questioning their capacity of law enforcement and are consequently more likely to impose administrative sanctions, rather than wasting time and resources transferring cases to the PSB, whenever they face difficulties in calculating the value of infringing products.[680]

The second obstacle relates to the collection of evidence. Transferring cases that meet the criminal liability threshold requires proof or direct physical evidence in the form of receipts, accounts, ledger books, or tax documents. Most PSB authorities will require such evidence before proceeding any further with a criminal investigation.[681] This burden of proof creates a significant difficulty for administrative agencies because most counterfeiters do not keep physical records of their activities, and any records recovered are written in a way intended to disguise counterfeiting.[682] For practical reasons, therefore, the PSB accepts cases for investigation only if the sums involved are particularly high, if serious issues of corruption exist, or in the event of death or serious injury to consumers – none of which applies in the usual circumstances facing a trademark.[683]

The third obstacle is that administrative agencies lack the incentive to initiate a case transfer. As explained in the discussion on the competition between the QTSB and AIC, the fines imposed by administrative agencies have been an unusually important source of extra-budgetary income since these agencies became financially independent after the decentralization reform. Thus, the chief incentive for an administrative agency to hold on to a case is that transferring it to the PSB would mean foregoing the opportunity to impose a fine on the violator. In 2005, for example, the SAIC collected 342 million yuan (about US$ 42 million) in fines imposed in cases of trademark counterfeiting.[684] IPR enforcement also costs

676 Shuwen Mei, 'Analysis on Conjunctive Rules of the IPR enforcement', Journal of National Prosecutors College, vol. 6, No. 2, 2008; Jiaping Ye, 'Problems in Conjunction between Administrative Enforcement and Criminal Enforcement in IPR Protection', *Science, Education and Culture*, April 2007.

677 Shuwen Mei, 2008; Jiaping Ye, 2007.

678 Shuwen Mei, 2008; Jiaping Ye, '2007.

679 Shuwen Mei, 2008.

680 Shuwen Mei, 2008.

681 Daniel C.K. Chow, 'Enforcement against Counterfeiting', 2000; Sandy Meng-Shan Liu, 2003.

682 Rory J. Radding, 'Enforcement of the Trademark Law in China', 11, Int'l Law Practicum 5, pp. 5-7, 1998.

683 Daniel C.K. Chow, 'Enforcement against Counterfeiting', 2000; Sandy Meng-Shan Liu, 2003.

684 Martin K. Dimitrov, 2009, p. 152.

administrative agencies resources for lodging, storing, and delivering confiscated goods. These costs cannot be recovered if the cases, along with the fines, are transferred to the PSB. The more such cases are transferred to the PSB, the less the administrative agencies can report in their annual enforcement statistics, and this in turn prevents them from asking for higher budgets from local and higher-level government authorities. A second and equally important explanation for the low transfer rate is the lack of negative incentives for the administrative agencies to coordinate with the criminal authorities: administrative officials are rarely punished for failure to follow the official rules that stipulate prompt and regular transfer of cases.

In short, problems demonstrated in IPR administrative enforcement, which is the most frequently utilized enforcement mechanism in China,[685] contribute significantly to ineffective IPR protection. Multiple administrative enforcers, with poorly defined IPR mandates, are the source of many problems, such as the low efficiency of enforcement and the shirking of enforcement responsibilities. More importantly, this situation creates competition in political interests, which encourages applying protectionist measures to IPR infringers and discourages the coordination and cooperation among IPR authorities that are indispensable for effective IPR administrative enforcement.

### 5.5.2 Problem of Local Protectionism – Horizontal Fragmentation

Local protectionism is another serious obstacle to effective IPR enforcement. In the 'IPR Protection Compendium 2006-2007', the State Council emphasized that 'local protectionism in the IPR protection, shielding IPR illegal or criminal activities, in particular practicing favoritism and not transferring the IPR criminal cases, should be sternly dealt with'.[686] The main cause of local protectionism in IPR protection is that many local municipalities in China rely on IPR infringement for their livelihood, and local governments have a direct or indirect economic interest in supporting counterfeiting and other related IPR-infringing activities. The involvement of local governments in the support of trade in IPR infringements makes effective enforcement at local levels difficult. Some local governments have invested millions of dollars in wholesale markets that sell counterfeits. Other local governments have formed private corporations to manage the sale and distribution of counterfeits. When all property was owned by the state under a planned economy, the dual roles of the government as

685 According to Bill Thompson, senior managing director of Pinkerton China, which investigates product fraud across the country, less than 1% of all counterfeiting cases reported are prosecuted. Ted Anthony, 'Made in China, or is it?' The Washington Times, 23 April 2002. See also Amanda S. Reid, 'Enforcement of Intellectual Property Rights in Developing Countries: China as a Case Study', *Depaul-LCA Journal of Art and Entertainment Law*, Spring 2003.

686 Article 4, 'IPR Protection Compendium 2006-2997', issued by the State Council in March 2006.

entrepreneur and regulator dominated the marketplace.[687] Under a mixed or transitional economy, however, in which private parties control substantial amounts of wealth and property, the government may be tempted to benefit its entrepreneur status by exploiting its role as both regulator and enforcer.[688] By creating distribution channels that manufacture, sell and deliver faked goods to retail markets and consumers, local governments often have a financial stake in the very counterfeiting activity that they are meant to suppress.[689] By owning, regulating, and operating wholesale distribution centers, local government officials lease shops to wholesalers and distributors who may also be potential counterfeiters.[690]

In addition to local government's involvement, the importance of counterfeiting or piracy to local economies also hinders the enforcement of government decisions to enforce IPR strictly. Shutting down trade in counterfeit goods would have serious negative repercussions for the local economy. Any serious crackdown would also affect the legitimate businesses that support counterfeiting, such as transportation and hotels, and this could result in the shutdown of the entire local economy – creating unemployment, social turmoil, chaos and unrest. By providing work for otherwise unemployable members of the local population, trade in counterfeited goods has become the lifeblood of some local economies and a significant source of income on which entire villages' continued survival and growth depend.[691] In Yiwu municipality, Zhejiang province, for example, one of the largest distribution centers for counterfeits, many laid-off workers have become 'counterfeit entrepreneurs'.[692] The local economy, with a staggering annual turnover of two billion US dollars,[693] is largely dependent on the influx and outflow of manufactured goods, many of which are trademark-infringing products. The name 'Yiwu' has become synonymous with a 'local government-protected counterfeiting center gone amuck'.[694] Thus, when faced with a choice between a set of laws from the central authority forbidding IPR infringements and the tremendous profits to be generated from local counterfeiting enterprises, local governmental officials may have more incentive to prioritize income and local economy resources over IPR protection.

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687 USTR Keeps China under 'Section 306' Monitoring – Except from 2002 Intellectual Property Protection Report, State Dept. Press Release and Documents, 1 May 2002, available at 2002 WL 25970050; Daniel C.K. Chow, 'Enforcement against Counterfeiting', 2000.

688 State Dept. Official Cites Intellectual Property Benefits – Wayne Says More Countries Protect Patents, Trademarks, State Dept. Press Releases and Documents, 23 April 2002, available at 2002 WL 25969744. See also Sandy Meng-Shan Liu, 'After WTO Accession: China's Dilemma with the Trafficking of Fakes', *The Trademark Reporter*, September-October 2003.

689 USTR Keeps China under 'Section 306' Monitoring – Except from 2002 Intellectual Property Protection Report, State Dept. Press Release and Documents, 1 May 2002, available at 2002 WL 25970050; Daniel C.K. Chow, 'Enforcement against Counterfeiting', 2000.

690 Daniel C.K. Chow, 'Enforcement against Counterfeiting', 2000.

691 Sandy Meng-Shan Liu, 2003.

692 Andrew Mertha, 2005, p. 172.

693 Statistics of Yiwu, turnover is 1,560,831 yuan in 2002and 1,884,856 in 2003, http://www.stat-yw.gov.cn/tjnj/2004/003-5.asp

694 Andrew Mertha, 2005, p. 172.

Needless to say, local authorities are also under pressure to implement central laws, and especially to respond when the central authority organizes an anti-counterfeiting or anti-piracy campaign. However, once the pressure is alleviated, for example when the campaign is over, the IPR infringement may return to the status quo. It is interesting to see, therefore, that the same administrative agency that may hinder effective IPR enforcement by providing or renting venues for outlet stores, stalls or warehouse spacing for the counterfeiters can under certain circumstances also play a role in enhancing and improving it.[695]

The dilemma faced by local authorities is described as 'overlapping', which is a feature shared by societies in transition.[696] Overlapping occurs when administrative agencies or other legal structures give the appearance of autonomy, but are in fact deeply enmeshed in and cross-influenced by remnants of the traditional social, economic, religious and political system.[697] An example of this would include a local law enforcement official legally obliged to shut down a factory for producing counterfeited goods.[698] The official, however, may have overlapping interests if the factory is also the main source of income for the village.[699] During IPR enforcement, the administrative authorities may face recalcitrance from villagers who are economically dependent on the counterfeiting factory. According to an officer of the QTSB investigation team, villagers try all means to undermine the IPR enforcement.[700] In one IPR enforcement, two QTSB officers uncovered an underground workshop for faked tobacco in a small village. They sealed up all the faked tobacco that was marked with counterfeited trademarks and contacted their colleagues to send a van to confiscate the products.[701] Before the van arrived, however, all the villagers, more than 200 people in total and including old people and children, rushed out, looted the tobacco and destroyed or hid it within a few minutes.[702] Without the proof, i.e. the faked tobacco, it was procedurally impossible to finalize the enforcement and impose fines on the owner of the workshop.[703] Although there are legal provisions prohibiting any activity that impedes administrative enforcement, it would be extremely difficult to impose punishment on those villagers for at least two reasons: firstly the lack of detailed guidelines for such punishment, and the fact that enforcing the punishment in the form of fines or detention, for example, would also be difficult and costly; and secondly there were such large numbers of people involved in this

695 Andrew Mertha, 2005, p. 4.
696 Amanda S. Reid, 2003.
697 Fred W. Riggs, 1964; Amanda S. Reid, 2003.
698 Amanda S. Reid, 2003.
699 Amanda S. Reid, '2003.
700 Interview with QTSB official in Guangdong province, 7 November 2005.
701 Interview with QTSB official in Guangdong province, 7 November 2005.
702 Interview with the QTSB official in Guangdong province, 7 November 2005.
703 Interview with the QTSB official in Guangdong province, 7 November 2005.

case and the belief that 'law cannot take actions against the masses' (*fabu zezhong*) is still widely accepted throughout Chinese society.[704]

Local officials facing a choice between disobeying directives from the head of the local government who can arrange job transfers, salary cuts and termination of employment, and disobeying directives from a higher-level unit unable to sanction misbehavior, tend to choose to protect local interests.[705] Under this fractured government structure, therefore, local officials have the autonomy to view national campaigns against counterfeiting as rather nebulous and abstract and not relevant to their localities or special circumstances.[706] Such powerful regionalism serves effectively to neutralize national efforts at copyright enforcement.

## 5.6 LIMITED ROLE OF JUDICIAL ORGANS IN IPR JUDICIAL REVIEW

As discussed in Chapter V, unjustifiable subordination of judicial organs to political and administrative organs constitutes an institutional obstacle to independent judicial review in China, and the limited scope of judicial review technically hinders courts from conducting an effective judicial review of specific administrative actions. This section examines how these problems impede judicial review of IPR cases, which is supposed to play an important role in IPR enforcement by redressing disputed administrative decisions.

### 5.6.1 Lack of Independence: Enough Judicial Review for IPR Administrative Decisions?

Local protectionism in IPR enforcement is particularly evident since, in many instances, local governments have a direct economic interest in supporting counterfeiting and pirating business. Due to the control and influence exerted by political and administrative authorities on courts at local levels, it is hard to preclude the possibility that courts may also be affected, to a certain extent, by the protectionism and may show partiality to counterfeiters in IPR judicial enforcement. A court's performance in IPR judicial review cases probably provides the best angle, when administrative actions are challenged, for demonstrating whether the court can resist interference and conduct an independent judicial review. In theory, if courts

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704 Interview with the QTSB official in Guangdong province, 7 November 2005. '*Fabu zezhong*' is a traditional saying in China, meaning laws are not laid down to punish the majority. It is of particular relevance in modern China, given that consciousness of the law remains low, especially among people living in small villages. Legal punishment would be neither efficient nor feasible in many circumstances in rural China, such as the tobacco looting case, until a wider acceptance of the value of the law.

705 Sandy Meng-Shan Liu, 2003; Daniel C.K. Chow, 'Enforcement against Counterfeiting', 2000.

706 Maria C.H. Lin, 'China after the WTO: What You Need to Know Now', 817 *Practicing Law Institute: Commercial Law and Practice*, 2001, pp. 177 and 205.

are under pressure and interference from administrative authorities in judicial review is general, there is no reason to expect any exception for courts in IPR-related judicial review cases. In practice, however, it is difficult to prove whether and to assess the extent to which courts experience interference by administrative or political authorities in IPR judicial review cases. Two possible proxies are the numbers of IPR judicial review cases; these show, to certain extent, whether individuals regard judicial review as a routine and reliable mechanism for challenging unsatisfied administrative IPR decisions, and also the success rate in such cases.

This investigation, however, is impeded by the lack of published statistics on nationwide IPR judicial review cases before 2009. According to Dimitrov's comprehensive study published in 2009, considerably fewer than 1% of the copyright and trademark administrative enforcement actions carried out by IPR agencies were subject to control through administrative reconsideration and administrative litigation.[707] The Supreme People's Court issued the first annual report on 'Intellectual Property Protection by the Chinese Court' in 2009.[708] According to this report, the role of the court in redressing IPR administrative actions was greatly enhanced in 2009. It states that the total number of IPR judicial review cases increased by 92.92% compared to 2008, with an increase of 19.03% in patent-related judicial review cases and an increase of 184.3% in trademark-related judicial review cases. Given the lack of statistics on the numbers of IPR administrative enforcement actions in the whole country, which are necessary in order to see how often IPR administrative enforcement actions are challenged, the information on the numbers of and increases in IPR judicial review cases revealed in this report is not useful in terms of helping to understand whether judicial review has become a strong tool in controlling IPR agencies.

After careful examination, the data in this report were found to be quite misleading. The report states that, in 2009, a total of 2072 first-instance IPR judicial review cases were received by local courts, including 688 cases relating to patents, 1376 to trademarks and 4 to copyright. At the same time, the Supreme People's Court received 54 IPR judicial review cases. The report also specified that the Beijing First Intermediate People's Court, which has jurisdiction over all first-instance IPR judicial review cases in Beijing, received 626 cases relating to patents and 1346 cases relating to trademarks. This means that only 62 and 40 judicial review cases, in patents and trademarks respectively, were received by all the other local courts together outside Beijing. In other words, 90.9% of patent-related judicial review cases and 97.8% of trademark-related judicial review cases in China in 2009 took place in the Beijing First Intermediate People's Court.

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707 Martin K. Dimitrov, 2009, p. 40.

708 'Intellectual Property Protection in Chinese Courts 2009', The Supreme People's Court, April 2010.

**Table 11: Distribution of IPR Judicial Review Cases in Chinese Courts in 2009[709]**

| | Number of Cases in All Local Courts | Number of Cases in Beijing Court | **Number of Cases in Other Local Courts** |
|---|---|---|---|
| Patent Judicial Review Cases | 688 | 626 | **62** |
| Trademark Judicial Review Cases | 1376 | 1346 | **30** |
| Copyright Judicial Review Cases | 4 | N/A | **N/A** |

As the above table indicates, all the other local courts in China outside Beijing received in total only 62 patent judicial review cases and 30 trademark judicial review cases in 2009. The report does not include statistics on copyright. Although the increase in the number of IPR judicial review cases referred to in the report seems impressive at first glance, Beijing accounted for the vast majority of the change. IPR judicial review in China turns out mainly to be a judicial review of two IPR authorities in Beijing: the Patent Re-examination Board under the SIPO, and the Trademark Appeal Board under the SAIC. It should be noted that the SIPO and SAIC are the only authorities in the whole country with responsibility for patent applications and trademark registrations respectively. IPR authorities at local levels deal only with patent or trademark infringements. This means that all disputed administrative decisions regarding patent applications and trademark registrations will be reviewed only by the court in Beijing, which has jurisdiction on judicial review cases against these two IPR authorities. This is why judicial review cases conducted by the court in Beijing account for such a large portion of all judicial review cases in China. In a country, however, where trademark infringement is rampant at all local levels, the severe imbalance in the distribution of IPR judicial review cases (i.e. 97.8% at the central level and only 2.2%, all of which relate to trademark infringements, at local levels) strongly suggests that IPR administrative authorities at local levels outside Beijing are rarely challenged by judicial organs.

The unreasonably low number of IPR judicial review cases in local courts demonstrates that, despite being available as a remedy in law, judicial review is far from being a regular and effective mechanism utilized by individuals as a remedy for unsatisfied IPR-related administrative decisions in practice. Although there is no direct evidence, the underutilization of judicial review could be suspected of being partially attributable to individuals' general lack of confidence in judicial organs' effectiveness in redressing administrative decisions. While improvements are starting to take place at the central level, judicial review by local courts, which are much more susceptible to interference from local governments, is underdeveloped and fails to perform its proper function. This once again proves that judicial organs' lack of independence, as an institutional barrier, can severely undermine the role that courts should play in judicial review.

709 'Intellectual Property Protection in Chinese Courts 2009', The Supreme People's Court, April 2010.

## 5.6.2 Case study – Problems of Limited Scope of Review and Arbitrary Application of Law

As discussed in Chapter V, courts' inability to review the legality of administrative decrees on which problematic administrative actions are based constitutes a major obstacle to the effectiveness of judicial review, as well as to the consistency of local rules and their implementation in China. The problem of the limited scope of review, which results in the existence of non-corrected conflicting legal provisions, is also clearly evident in IPR cases.

In April 2003, a trademark infringement case was brought before the intermediate court of Hangzhou by Colgate-Palmolive Company (Colgate Company) against Dingxin Paper Company of Hangzhou (Dingxin Company), which was alleged to have produced 22,000 packing cases of Colgate toothpaste without authorization. Colgate Company claimed that the defendant should stop its infringing activity, apologize publicly and compensate Colgate Company for its economic loss in the amount of 1,297,194 yuan. The court confirmed the defendant's infringing activity and accepted the claims for the infringement to be stopped and for a public apology. With regard to compensation, however, the court rejected the method of calculating the economic loss proposed by the plaintiff and ruled that the defendant should pay compensation of only 300,000 yuan.

### *5.6.2.1 Limited Scope of Review – Problem of Conflicting Legal Provisions*

Before bringing the litigation before the court, the Colgate Company filed a complaint for administrative enforcement with the QTSB of Hangzhou city. As mentioned before, the QTSB at local levels is concurrently in charge of trademark enforcement based on local regulations, despite the fact that the Trademark Law designates the AIC as the competent authority for trademark enforcement. As regards the QTSB's jurisdiction on IPR enforcement, the court made conflicting statements in its judgment. In one fact statement, the court stated that 'for the reason that the QTSB, in contrast to the AIC, is not empowered to impose compensation for infringing activity under the Trademark Law, the plaintiff filed its litigation with the court for civil compensation.' In another fact statement, however, the court contradictorily affirmed that the QTSB of Hangzhou city had imposed the penalty decision on the defendant, confiscating its illegal earnings of 68,000 yuan and imposing a penalty amounting to two times the illegal earnings. The court on the one hand accepted that the QTSB was *de facto* enforcing the penalty right in trademark infringement, and on the other denied this right *de jure*. It provided no further explanation of this issue. Whether the QTSB can, according to the law, be the competent authority imposing administrative penalties on trademark infringements therefore remains unclear.

Courts are best placed to supervise and rectify conflicting laws and regulations in order to ensure a consistent legal system and uniform legal application. If courts are not allowed to review the legality of laws and regulations, the many conflicting legal provisions cannot

be corrected expeditiously through judicial legal application. This case shows an apparent contradiction between the provisions in the 'Implementing Rule of the Trademark Law' and the provisions in the 'Trademark Law' regarding the compensation rule. For infringements where the damage is hard to estimate, the Trademark Law requires the compensation to be less than 500,000 yuan, whereas the Implementation Rule of the Trademark Law specifies that the compensation shall be less than 100,000 yuan.[710] In the Colgate case, the court adopted the rule in the Trademark Law, without mentioning the provision in the Implementation Rule of the Trademark Law. It simply ignored such a striking legal contradiction between the 'law' issued by the NPC and the 'administrative regulation' issued by the State Council. Contrary to what is required by law, it also failed to report the conflict to the SCNPC. Deprival of the right to review the legality of legal enactments would seem to bring the court into the status of 'nonfeasance' in supervising the consistency of laws. Ignorance, nonfeasance and even sometimes self-contradictory statements in judgments, as manifested in this case, mean not only that conflicting legal enactments will remain unresolved, but also that the gap between law on paper and law in practice will intensify.

#### *5.6.2.2 Arbitrary Application of Law – Difficulties in Estimating Compensation*

The main dispute in this case concerned the estimation of compensation. According to the Trademark Law, compensation should be calculated based on either the economic loss of the IPR holder or the benefits earned by the infringer.[711] The plaintiff claimed that its economic losses should be calculated based on the profit that could be made from every 50 grams of Colgate toothpaste, noting that every packing case counterfeited by Dingxin Company normally contained 72 tubes of Colgate toothpaste, each of 50 grams. The court rejected this claim and ruled that the profits that would have been made from genuine Colgate toothpaste had no connection with the plaintiff's losses, and accordingly could not be used as a reference for estimating the compensation. Given that the plaintiff did not provide any effective proof either of the loss it suffered as a result of the counterfeited packing cases or of the benefits that the defendant earned through the counterfeiting, it was up to the court to decide on the amount of compensation.

In this case, the court specifically cited Article 56 of the Trademark Law, which provides that 'when the economic loss of IPR holders or the benefit earned by the infringer is difficult to define, the court can impose compensation, according to the circumstances, of less than 500,000 yuan'. This provision can be viewed as an exception to the general rule on compensation provided for in the Implementing Rule of the Trademark Law, which specifies that 'if the damages can be identified, the compensation should be less than three times the illegal business turnover of the infringers'.[712] Due, however, to the lack of comprehensive

710 Article 52, Implementation Rule of the Trademark Law, issued in August 2002.

711 Article 56, Trademark Law, issued in August 1982, revised in February 1993 and October 2001.

712 Article 52, Implementation Rule of the Trademark Law, issued in August 2002.

guidance on means of estimating the remedy, many cases will in practice fall into the category of 'cases in which loss or benefit is difficult to calculate'. If the potential profits that may be generated from genuine products compared with the same amount of counterfeited ones cannot be adopted as a reference, it will be extremely difficult to calculate the IPR owner's economic loss. In addition, the infringers will not normally keep any relevant documents or receipts of their business,[713] thus it is scarcely possible for the IPR holder, on whom the burden of proof rests, to calculate the benefits earned by the infringers. In this case, the court did not specify how the compensation of 300,000 yuan was calculated. Obviously, this amount was far less than the plaintiff expected. Although the general rule on estimating compensation seems more reasonable because it makes the amount of the remedy dependent on the scale of the infringing business turnover, the difficulties existing in the vague legal provision on estimating compensation, which allow excessive discretion to the courts, mean that the exceptional rule is applied more frequently. If the 'less than 500,000 yuan' penalty were to apply to all infringing cases where damage was difficult to determine, one consequence could be that the more serious the infringement or the more complicated the case, the less compensation there will be.

The court also rejected the plaintiff's claim of 'business reputation loss'. The plaintiff claimed that since Colgate is a well-know trademark, the counterfeited packing cases made by the defendant, which would ultimately bring large volumes of fake Colgate toothpaste into the Chinese market, would cause a huge loss to its business reputation, and the defendant should thus compensate this loss by paying compensation of 500,000 yuan. The court denied compensation for the loss of reputation by ruling that the trademark right was by its nature a property right, rather than a personal right, and therefore the compensation for the loss of business reputation should be limited to the actual loss of property. There should therefore be no separate compensation for 'reputation' beyond the compensation for business loss. Whether the 'business reputation loss' will be compensated in trademark-infringing cases remains an open question since there is a lack of relevant legal provisions on this issue.

Being able to estimate compensation is essential for IPR enforcement in China. Inadequate remedies do not constitute an effective deterrent to IPR infringement. The lack of precise legal rules and precedents mean a court may apply the law and decide on the amount of compensation arbitrarily. As demonstrated in the above case, the court's assessment on compensation is rather subjective and lacking reasoning, while the amount is not enough to deter the IPR infringer. Allowing courts too much discretion in deciding on remedies may be convenient for reasons of local protectionism, especially when local courts are already quite susceptible to local governments. This problem also leads to uncertain and inconsistent application of IPR laws, which results in very varied levels of IPR protection within China.

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713 In this case, for example, the defendant (Dingxin Company) did not keep any documents or receipts relating to the counterfeited packing cases.

In summary, the perennial problem of rampant IPR infringement in China demonstrates that its IPR enforcement is not effective. Despite its high volume, the quality of enforcement is low and so does not act as a deterrent to further infringement. As discussed, the remedies provided by administrative authorities are far from adequate as a deterrent, while remedies decided by courts in judicial enforcement are arbitrary and inconsistent. Whereas the central authority demonstrates strong purpose in seeking to enhance IPR protection, actual enforcement at local levels is undermined by various institutional obstacles. Since the enforcement provisions in TRIPS are too general and ambiguous, it remains technically difficult to challenge China under these provisions for its general ineffective IPR enforcement. Moreover, even if the DSB could make such a finding, it would be extremely difficult for China to implement such a ruling since this would require structural changes in China's judicial and administrative systems. In this regard, TRIPS creates dilemmas for its own regulations. On one hand, TRIPS states that it does not give rise to any obligation for adjustments in the enforcement of law in general;[714] on the other hand, institutional changes are indispensable if China is to achieve effective IPR enforcement and become TRIPS-compliant.

## 5.7 CONCLUSION

The difficulties found in China's compliance with systemic obligations have contributed significantly to its ineffective IPR enforcement. Firstly, transparency in the field of IPR protection does not differ from the general problematic transparency in China's regulatory regime. IPR-related laws, regulations, and judicial decisions are only selectively published, and there is no one journal or website that has been established for public access purposes. Lack of transparency makes it difficult to scrutinize the consistency of application of IPR laws and is also a main contributor to unpredictable and capricious administrative IPR enforcement. Secondly, the difficulty demonstrated in the problem of national regulation and fragmented authority is a prominent issue in IPR enforcement and leads to poorly coordinated IPR enforcement at two levels: the horizontal level of cooperation between various IPR enforcing authorities, and the vertical level of cooperation between central government and local governments. It has a detrimental effect on the effectiveness of IPR enforcement, which is contingent on a high degree of cooperation. Thirdly, due to structural defects in judicial organs, judicial review is far from becoming a mechanism regularly utilized by individuals as a remedy for unsatisfied IPR-related administrative decisions. The majority of IPR-related judicial review cases take place at the central level, while the number of cases at local levels is extremely low. This clearly suggests that IPR-related administrative decisions are rarely challenged by judicial organs, and thus judicial review by local courts, which are more susceptible to interference from local governments, fails to perform its proper function.

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714 Articles 41.5 and 1.1, TRIPS.

The TRIPS Agreement plays a perplexing role in inducing compliance with its enforcement requirements. Its ambition to reconcile interests of countries at various different stages of development makes it sacrifice enforceable provisions on enforcement. The ambiguous wording and the general clause hinder it from becoming an effective framework to ensure enhance IPR enforcement, especially by a country such as China. The substantial institutional impediments mean that the costs to China of compliance have probably been underestimated. Since TRIPS and international pressure arguably have little effect on weak IPR enforcement, more focus should be put on internal conditions in China. While external impact can still be a useful supplement, internal impetus or motivation to change should serve as the primary force for the institutional reforms that are crucial for enhancing IPR enforcement with a long-term effect.

# Chapter 6

## Conclusion

China's integration into the world trading system has been a slow and arduous process. Adaptation of its domestic institutions and legislative framework is being hindered by difficulties relating to its compliance with systemic WTO obligations. Problems generated by problematic institutional and legal conditions in China, which remain largely unchanged, as demonstrated in the review reports prepared by the WTO and the US, have persisted throughout its ten years of WTO membership. China is therefore under constant pressure to build an improved institutional framework within which better compliance with many substantive WTO obligations can be achieved. However, the pressure exerted on China by its trading partners, in bilateral meetings or at the WTO, has failed to bring about any of the desired results. One important reason for this failure is that the difficulties for China in achieving the required improvements in domestic regulatory conditions have been under-recognized. As demonstrated in this study, the problems in adapting to a legal system that is compatible with the WTO commitments are deeply rooted in China's complex, distinct and politicized domestic regulatory context. The *difficult and complicated situation* in China is unlikely to be changed by the approaches that are currently being utilized by its trading partners.

The main difficulty in complying with the transparency requirement lies in China's legislative structure and its distinct legal culture. Firstly, legislative power has been diffused to multiple levels of agencies, not only to legislative bodies but also to administrative agencies at local levels. Although the hierarchy of legislative authorities and their legal enactments appears clear at a central level, the legal status of legislative enactments adopted by local authorities is vaguely defined, and this is a main contributor to the problem of non-transparency in Chinese legislation. The lack of an effective scrutiny mechanism means that conflicts between legal documents are left unresolved, and this leads to chronic disarray in China's formal legal system.

Secondly, beyond the formal legal system, there exists a set of informal 'laws' referred to as normative documents. Although not recognized as a formal source of law by any Chinese law, they are frequently adopted by administrative agencies at local levels for legal regulation purposes. The main problem that normative documents create for transparency is that their adoption is largely arbitrary, with no due process regulation, and the documents themselves are not usually publicly accessible. The publication requirements provided in China's Legislative Law, for example, are simply not applicable to normative documents since they are not the subjects of the regulation.

Thirdly, the liberal principle of government accountability ('government is an agency of popular will'), from which the concept of transparency derives, is not readily evident in Chinese legal culture. In China, by contrast, law is an agency of the will of the government or the Party in that governance is pursued by a sovereign political authority that remains largely immune to challenge, while regulatory norms serve as instruments of the Party's policy of control, and the supremacy of the Party remains. Under this ideology,

administrative agencies have responsibilities *for* society, but are not responsible *to* it. They are accountable only to their political superiors. This distinct legal culture weakens the norm of government accountability, and the importance of transparency, which is based on the norm of government accountability, is consequently also weakened. The wide and irrational existence of informal legal sources verifies the strong influence of this legal culture in China: the Party and government rely largely on flexible and policy-like laws on governance and they, rather than the role of law, continue to enjoy supremacy of power in the country. Hindered by institution-related difficulties, trading partners' efforts to urge China to institute a single nationwide journal for publication of all trade-related laws, regulations and rules can therefore achieve only limited results at a central level and much less at local levels.

The problem of central-local relations also constitutes an institutional obstacle to uniform administration of the implementation of law. Although China constitutionally remains a unitary state from a formal institutional perspective, power is, in a practical and behavioral sense, divided between the center and the localities. This fragmented nature of the country is visible throughout society and creates a general difficulty in national regulation. The decentralization reform launched in the 1980s encourages local autonomy in order to create an incentive to maximize local economic growth. In this process, the central authority traded a substantial degree of regulatory and policy-making power in exchange for rapid industrialization. The increase in local discretion and decline in central control have undermined national governability. Moreover, the fragmented legal system, reflected in conflicting and vaguely defined legal sources, and arbitrary and under-regulated legal implementation by local administrative authorities, also creates additional difficulties for uniform administration by the central authority.

An illustrative example of the fragmented nature of state administration is the problem of market fragmentation, i.e. a single market with free flow of trade is absent or highly deficient in China. Various domestic trade barriers, which may be similar in form to international trade barriers and include both technical barriers and quantitative restrictions, are widely utilized by local governments in order to restrict the market access of products from other localities and to protect their own economic development. China's domestic market acts differently from what could be expected of a political union with a centralized government. Although it has a common external policy, the country does not have an integrated internal market. International trade increases simultaneously with decreases in internal trade. For the purpose of a unified domestic market and fair competition the central government has made some legislative efforts to eliminate internal trade barriers. However, the legislation has not been effectively enforced at local levels and has thus failed to put an end to local trade barriers. While the market fragmentation can be attributed to various factors in the country's economic and administrative systems, its continued existence demonstrates, to a large extent, the central government's inability to achieve uniform administration of application of the central law. The lack of a single market causes considerable trade distortions and hinders China from complying with substantive WTO obligations. It deprives the country of

the possibility to review trade measures in accordance with non-discrimination rules since Chinese domestic products are already subject to discriminatory treatment, and thus leaves the rule of national treatment a dead letter. The problem of market fragmentation also manifests itself in tension between the central government's pursuit of national regulation and its wish to encourage local autonomy for the sake of economic development. WTO membership intensifies this tension by requiring China to decentralize more economic activities to local government – for instance, foreign investment measures – while at the same time ensuring uniform administration and being able to regulate local activities.

The function of judicial review is to enhance uniform implementation of laws by allowing individuals to challenge administrative decisions at a domestic level. In China, this is undermined by structural defects in the judicial organs. As a mechanism developed in Western countries, judicial review is essentially concerned with the checks and balances exercised by the judiciary over the other branches of a state. It is built upon fundamental principles, such as the concept of the rule of law and the separation of powers. However, these principles find little resonance in China. There is no separation of powers in China and, to some extent, judicial organs are subordinated to administrative and Party organs. Contrary to what is stated in the Chinese Constitution, the Party possesses the highest power; this power is often exercised by administrative authorities, which can thus exert effective influence over judicial organs. The general problem of a non-independent judiciary is particularly evident in respect of judicial review where administrative agencies are challenged. In addition to experiencing external interference from administrative and Party organs, courts often opt to exercise self-restraint in judicial review cases in order to avoid confrontation with administrative authorities. The extraordinarily high withdrawal rate of judicial review litigation in China points to how courts conduct this voluntary restraint: they may persuade plaintiffs to drop a case by suggesting that there is low chance of winning and that out-of-court settlement would be a better solution.

Moreover, the limited scope of judicial review exacerbates the problem caused by the structural defects. Courts are not able to review the legality of administrative decrees. China's exclusion of administrative decrees from the scope of judicial review is a unique practice, even though primary legislation is not subject to judicial review by ordinary courts in most legal regimes. In many cases, reviewing the legality of administrative decrees is essential in order to review the legality of administrative decisions based on those decrees. The limited scope of review technically hinders courts from providing an effective review of problematic administrative decisions.

At the request of the WTO members, China has endeavored to provide a special rule for judicial review of administrative decisions relating to international trade by, for example, enhancing the jurisdictional level from basic courts to intermediate courts, which may have more knowledgeable judges and are less susceptible to local interference. The fact that little data could be found suggests that this special rule is rarely applied. It may be easy for

China to promulgate a rule as temporary relief for trading partners, but this will be hard to put into practice and is unlikely to achieve significant results in the long term. None of the difficulties found in this study will be resolved by the special rule, and foreign trade-related administrative decisions will still be reviewed under the framework of major relevant Chinese legislation, which means, for example, that the scope of the review will remain limited. It is thus neither rational nor realistic to request China to establish an insulated and preferential system specifically for international trade matters.

The case study of China's ineffective IPR enforcement demonstrates how the difficulties found in compliance with the systemic obligations impede the effectiveness of substantive WTO rules. Firstly, transparency, which plays an important role in ensuring certainty of IPR enforcement, remains weak in China. IPR-related laws and regulations, as well as judicial decisions, are only selectively published, and there is no one journal or website that has been established for public access. Lack of transparency makes it difficult to scrutinize the consistency of application of IPR laws and is also a main contributor to unpredictable and capricious administrative IPR enforcement.

Secondly, the fragmentation problem undermines the effectiveness of IPR enforcement, mainly because the latter is contingent on high degree of cooperation between regions and departments. Cooperation between departments is hindered by vertical fragmentation, i.e. numerous authorities with vaguely defined and overlapping jurisdiction have competence on IPR enforcement. The dispersed competency leads to a problem of shirking of enforcement responsibilities in some cases, and duplicative and uncoordinated enforcement in others. Difficulties of cooperation between departments are also evident when cases have to be transferred from administrative agencies to public security bureaus for criminal enforcement. These impede criminal enforcement from becoming an effective remedy for IPR infringement. Cooperation between regions is hindered by horizontal fragmentation, which mainly refers to the problem of central-local relations and local protection in IPR enforcement. Economic reliance on the IPR infringement industry motivates local governments to allow their own economic interests to prevail over IPR protection. At the same time, the fragmented state administration structure allows local governments autonomy to neutralize national efforts in IPR enforcement. IPR infringement may simply return to the status quo once a national campaign is over.

Thirdly, the examination of IPR-related judicial review cases demonstrates that, due to structural defects in judicial organs, judicial review is far from becoming a mechanism regularly utilized by individuals as a remedy for unsatisfied IPR-related administrative decisions. The majority of IPR-related judicial review cases in China take place at the central level, while the number of cases at local levels is extremely low. In a country where trademark infringement is rampant at all local levels, there were only 30 IPR-related judicial review cases at local levels in 2009. Although it is difficult to establish the exact extent to which the problem of the lack of independence undermines the effectiveness of

judicial review, the extremely low number of cases strongly suggests that, at local levels, IPR-related administrative decisions are rarely challenged through judicial review. Judicial review conducted by local courts, which are more susceptible to interference from local governments, fails to perform its proper function.

Trading partners need to be aware of the institution-related difficulties in China's IPR enforcement if they are to formulate a feasible strategy for enhancing enforcement. China has lowered the threshold of criminal liability for IPR infringements, as requested by the US in WTO dispute settlement proceedings. However, difficulties in transferring cases that meet the threshold from administrative authorities to criminal enforcement authorities have meant that the desired goal of making more IPR-infringing activities subject to criminal enforcement could not be achieved.

The complexity of Chinese legislation, the fragmented nature of the administrative system and the structural defects in judicial organs constitute formidable obstacles to China's compliance with systemic WTO obligations. Understanding the institutional impediments faced by China makes it easier to understand that imposing WTO-plus obligations on China is an irrational strategy and unlikely to achieve the desired result since it requires a weaker member to comply more than other members. It would be naïve to think that the process of adaptation can be accelerated by exerting sufficient external pressure. The difficulties for China need to be fully recognized and their full implications understood. Comprehensive consideration of a member's institutional capacity to comply is the first step towards finding a solution for better integration. To be fully compliant with the systemic WTO requirements, China needs to undertake holistic institutional reform, which is unlikely to happen in the short term. In this regard, the more strict application of Article X demonstrated in a recent WTO case may not be a good tendency, given the threat that China's non-conformity could constitute to the trading system's normativity. China's difficult integration into the WTO also demonstrates that expanding the WTO mandate may not necessarily help the world trading system to optimize its effectiveness. Requiring compliance with those deeply intrusive rules by a member such as China pushes the limit of the WTO's governance capacity to maintain a balance between trade liberalization and national regulatory autonomy. It creates a dilemma for the WTO: whether to move forward by requiring stricter compliance with intrusive provisions in order to consolidate the expanded mandate, or whether to slow down by leaving those provisions vague and less intrusively applied in order to alleviate tension and retain its operation. How to resolve the dilemma and accommodate developing countries' strong legal and political constraints will be one of the most challenging tasks for reform of the world trading system in the future.

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# Summary

This thesis has explored legal difficulties existing in China's domestic institutions with regard to its WTO compliance, by looking at three specific systemic obligations provided in GATT Article X, i.e. transparency, uniform administration of implementation of law, and judicial review. It has been conducted within the framework of compliance theory of international law, which discerns compliance from implementation in a way that compliance goes beyond implementation by requiring national laws that incorporate international treaty obligations to be actually enforced at national level. In this theory, the importance of domestic institutions has been emphasized in ensuring ultimate effectiveness of international law.

The WTO contains a series of systemic obligations that impose requirements on domestic institutions. The highest concentration of these systemic obligations can be found in GATT Article X. Article X was not regarded as an essential requirement when it was drafted for the reason that it imposed no extra obligation for developed countries. The expansion of WTO's membership, as well as the expansion of its jurisdiction, transforms this article to be a more important requirement as a procedural guarantee for the effectiveness of WTO substantive obligations and a requirement that may entail systemic redesign for many less-developed countries. For a country like China, these systemic obligations require it not only to be bound by WTO rules, but also to make domestic conditions conducive to the rules' implementation. Due to the intrusive character of these obligations, however, this article has received little attention and been applied by the WTO DSB with a great caution. It presents a challenge for the WTO to make a balance between effectiveness of WTO rules and national regulation autonomy.

China's remaining obstacles to its compliance with WTO obligations after ten years of the accession are closely related to its problematic domestic institutional and legal conditions. Debates continue as to whether China has adequately complied with both the letter and spirits of its obligations. Although Chinese law in paper looks largely compatible with WTO obligations, the main obstacles exist in law in practice. It confirms with what has been suggested by compliance theory that enforcement of national laws is an essential second step in compliance with international law. This thesis uses Article X, which imposes immediate requirements on domestic institutions, as a lens to examine how domestic conditions could affect China's compliance and the effectiveness of WTO rules. The institution-related difficulties found in the compliance with Article X may cut across and impede implementation of trading rules in various trade areas, and thus represent the overall institutional obstacles to effectiveness of WTO rules. The aim of this thesis is to provide comprehensive understanding of China's institution-related difficulties in its WTO compliance as the first step to formulate a better strategy for China's integration; to put insight on the extent to which WTO DSB should enforce Article X in its future dispute settlement, and to shed some light on the limit of WTO's governance capacity.

Chapter two finds that the main difficulty in complying with the transparency requirement lies in China's legislative structure and its distinct legal culture. Firstly, legislative power

has been diffused to multiple levels of agencies, not only to legislative bodies but also to administrative agencies at local levels. Although the hierarchy of legislative authorities and their legal enactments appears clear at a central level, the legal status of legislative enactments adopted by local authorities is vaguely defined, and this is a main contributor to the problem of non-transparency in Chinese legislation. The lack of an effective scrutiny mechanism means that conflicts between legal documents are left unresolved, and this leads to chronic disarray in China's formal legal system. Secondly, normative documents, which exist beyond the formal legal system as a set of informal laws, are frequently adopted by administrative agencies at local levels. Their adoption is largely arbitrary, with no due process regulation, and the documents themselves are not usually publicly accessible. Thirdly, the liberal principle of government accountability ('the government is an agency of popular will'), from which the concept of transparency derives, is not readily evident in Chinese legal culture. In China, by contrast, law is an agency of the will of the government or the Party in that governance is pursued by a sovereign political authority that remains largely immune to challenge, regulatory norms serve as instruments of the Party's policy of control, and the supremacy of the Party remains. Under this ideology, administrative agencies have responsibilities *for* society, but are not responsible *to* it. They are accountable only to their political superiors. This distinct legal culture weakens the norm of government accountability. Consequently, the importance of transparency, which is based on the norm of government accountability, is also weakened. Hindered by institution-related difficulties, trading partners' efforts to urge China to institute a single nationwide journal for publication of all trade-related laws, regulations and rules can therefore achieve only limited results at a central level and much less at local levels.

As demonstrated in Chapter three, the central-local problem also constitutes an institutional obstacle to uniform administration of the implementation of law. Although China constitutionally remains a unitary state from a formal institutional perspective, power is, in a practical and behavioral sense, divided between the center and the localities. This fragmented nature of the country is visible throughout society and creates a general difficulty in national regulation. Moreover, the fragmented legal system, reflected in conflicting and vaguely defined legal sources, and arbitrary and under-regulated legal implementation by local administrative authorities, creates additional difficulties for uniform administration by the central authority. An illustrative example of the fragmented nature of state administration is the problem of market fragmentation, i.e. a single market with free flow of trade is absent or highly deficient in China. China's domestic market acts differently from what could be expected of a political union with a centralized government. Although it has a common external policy, the country does not have an integrated internal market. For the purpose of a unified domestic market and fair competition the central government has made some legislative efforts to eliminate internal trade barriers. However, the legislation has not been effectively enforced at local levels and has thus failed to put an end to local trade barriers. While the market fragmentation can be attributed to various factors in the country's economic and administrative systems, its continued existence demonstrates, to a large

extent, the central government's difficulty to achieve uniform administration of application of the central law. The lack of a single market causes considerable trade distortions and hinders China from complying with substantive WTO obligations. It deprives the country of the possibility to review trade measures in accordance with non-discrimination rules since Chinese domestic products are already subject to discriminatory treatment, and thus leaves the rule of national treatment a dead letter. The problem of market fragmentation also manifests itself in tension between the central government's pursuit of national regulation and its wish to encourage local autonomy for the sake of economic development. WTO membership intensifies this tension by requiring China to decentralize more economic activities to local government – for instance, foreign investment measures – while at the same time to ensure uniform administration and be able to regulate local activities.

Chapter four examines that the function of judicial review, which is to enhance uniform implementation of laws, is undermined by structural defects in Chinese judicial organs. As a mechanism developed in Western countries, judicial review is essentially concerned with the checks and balances exercised by the judiciary over the other branches of a state. It is built upon fundamental principles, such as the concept of the rule of law and the separation of powers. However, these principles find little resonance in China. There is no separation of powers in China and, to some extent, judicial organs are subordinated to administrative and Party organs. The general problem of a non-independent judiciary is particularly evident in respect of judicial review where administrative agencies are challenged. In addition to experiencing external interference from administrative and Party organs, courts often opt to exercise self-restraint in judicial review cases in order to avoid confrontation with administrative authorities. The extraordinarily high withdrawal rate of judicial review litigation in China points to how courts conduct this voluntary restraint: they may persuade plaintiffs to drop a case by suggesting that there is low chance of winning and that out-of-court settlement would be a better solution.

Moreover, the limited scope of judicial review exacerbates the problem caused by the structural defects and technically hinders courts from providing an effective review of problematic administrative decisions. Courts are not able to review the legality of administrative decrees. China's exclusion of administrative decrees from the scope of judicial review is a unique practice, even though primary legislation is not subject to judicial review by ordinary courts in most legal regimes. In many cases, reviewing the legality of administrative decrees is essential in order to review the legality of administrative decisions based on those decrees. At the request of the WTO members, China has endeavored to provide a special rule for judicial review of administrative decisions relating to international trade by, for example, enhancing the jurisdictional level from basic courts to intermediate courts, which may have more knowledgeable judges and are less susceptible to local interference. The fact that little data could be found in the application of the rule, suggests that this special rule is rarely applied. It may be easy for China to promulgate a rule as

temporary relief for trading partners, but this will be hard to put into practice and is unlikely to achieve significant results in the long term.

Through the case study of China's ineffective IPR enforcement, Chapter five demonstrates how the difficulties found in the previous three chapters may hinder China's compliance with WTO obligations at more concrete level. Firstly, IPR-related laws and regulations, as well as judicial decisions, are only selectively published, and there is no one journal or website that has been established for public access. Lack of transparency makes it difficult to scrutinize the consistency of application of IPR laws and is also a main contributor to unpredictable and capricious administrative IPR enforcement. Secondly, the fragmentation problem undermines the effectiveness of IPR enforcement, mainly because the latter is contingent on high degree of cooperation between regions and departments. Cooperation between departments is hindered by vertical fragmentation, i.e. numerous authorities with vaguely defined and overlapping jurisdiction have competence on IPR enforcement. The dispersed competency leads to a problem of shirking of enforcement responsibilities in some cases, and duplicative and uncoordinated enforcement in others. Cooperation between regions is hindered by horizontal fragmentation, which mainly refers to the problem of central-local relations and local protection in IPR enforcement. Economic reliance on the IPR infringement industry motivates local governments to allow their own economic interests to prevail over IPR protection. At the same time, the fragmented state administration structure allows local governments autonomy to neutralize national efforts in IPR enforcement. Thirdly, the examination of IPR-related judicial review cases demonstrates that, due to structural defects in judicial organs, judicial review is far from becoming a mechanism regularly utilized by individuals as a remedy for unsatisfied IPR-related administrative decisions. The majority of IPR-related judicial review cases in China take place at the central level, while the number of cases at local levels is extremely low. Although it is difficult to establish the exact extent to which the problem of the lack of independence undermines the effectiveness of judicial review, the extremely low number of cases suggests that, at local levels, IPR-related administrative decisions are rarely challenged through judicial review.

The complexity of Chinese legislation, the fragmented nature of the administrative system and the structural defects in judicial organs constitute formidable obstacles to China's compliance with systemic WTO obligations. Understanding the institutional impediments faced by China makes it easier to understand that imposing WTO-plus obligations on China is an irrational strategy and unlikely to achieve the desired result since it requires a weaker member to comply more than other members. It would be naïve to think that the process of adaptation can be accelerated by exerting sufficient external pressure. Comprehensive consideration of a member's institutional capacity to comply is the first step towards finding a solution for better integration. China's case demonstrates that expanding the WTO mandate may not necessarily help the world trading system to optimize its effectiveness. Requiring compliance with those deeply intrusive rules by a member such as China pushes the limit of the WTO's governance capacity to maintain a balance between trade liberalization and

national regulatory autonomy. How to accommodate developing countries' strong legal and political constraints will be one of the most challenging tasks for reform of the world trading system in the future.

# Samenvatting

*China's naleving van WTO systeem-verplichtingen*

Institutionele belemmeringen voor de effectieve uitvoering van Artikel X GATT

Dit proefschrift onderzoekt de juridische problemen die in binnenlandse instituties van China optreden met betrekking tot de WTO naleving. Daarbij wordt in het bijzonder aandacht gegeven aan drie specifieke systeem-verplichtingen in de GATT Artikel X, i.e. transparantie, uniforme administratie van de uitvoering van de wet en de rechterlijke toetsing. Het onderzoek is uitgevoerd in het kader van de *compliance* theorie die een onderscheid maakt tussen implementatie van verplichtingen, door uitvoering in nationale wetgeving, en daadwerkelijke afdwinging op nationaal niveau. In deze theorie wordt het belang van binnenlandse instituties bij het waarborgen van effectiviteit van het internationaal recht benadrukt.

De WTO bevat een reeks systeem-verplichtingen die eisen stelt aan binnenlandse instituties. Deze verplichtingen zijn vooral te vinden in het GATT Artikel X. Deze bepaling werd aanvankelijk niet beschouwd als een essentieel vereiste omdat het geen extra verplichtingen oplegde aan GATT-partijen. De uitbreiding van het aantal leden van de WTO geeft dit artikel echter nieuwe betekenis: een procedurele waarborg voor de effectiviteit van de WTO-inhoudelijke verplichtingen en een vereiste dat *systemic redesign* met zich mee kan brengen voor vele minder ontwikkelde landen. Voor China vereist binding aan Artikel X het scheppen van binnenlandse voorwaarden ter bevordering van de uitvoering van systeem-verplichtingen. Echter, vanwege het indringende karakter van de verplichtingen heeft dit artikel weinig aandacht gekregen en heeft de WTO DSB deze bepaling met grote terughoudendheid toegepast. Het vormt een uitdaging voor de WTO om een evenwicht te vinden tussen effectiviteit van de WTO-regels en de autonomie van de nationale regelgeving.

Tien jaar na China's toetreding zijn de resterende belemmeringen voor de naleving van de WTO verplichtingen nauw verwant aan de problematische binnenlandse institutionele en juridische omstandigheden. De discussie rond de vraag of China voldoende heeft voldaan aan zowel de letter als de geest van haar verplichtingen is geenszins afgerond. Hoewel de Chinese wet op papier grotendeels verenigbaar lijkt met de WTO-verplichtingen, zijn de belangrijkste belemmeringen te vinden in de uitvoeringspraktijk van de wetgeving. De praktijk bevestigt de stelling van de *compliance* theorie dat de handhaving van nationale wetgeving in overeenstemming met het internationale recht een essentiële tweede stap is. Dit proefschrift maakt gebruik van artikel X, dat onmiddellijke eisen oplegt aan binnenlandse instituties. Door de lens van Artikel X is onderzocht hoe binnenlandse omstandigheden de naleving en de effectiviteit van de WTO-regels kunnen beïnvloeden. De problemen gerelateerd aan de instituties, die zijn geconstateerd bij de naleving van artikel X, kunnen de uitvoering van handelsregels op diverse terreinen tegenwerken en daarmee aanzienlijke belemmeringen vormen voor de doeltreffendheid van de WTO-regels. Het doel van dit proefschrift is om inzicht te verschaffen in China's institutionele problemen bij

de naleving van de WTO-voorschriften. Een beter inzicht geldt als de eerste stap om een betere integratie van China in het wereldhandelssysteem te realiseren. Daarnaast geeft het proefschrift inzicht in de mate waarin de WTO DSB artikel X moet afdwingen bij het oplossen van toekomstige conflicten en werpt het licht op de beperking van de bestuurscapaciteit van de WTO.

Hoofdstuk twee stelt vast dat de voornaamste moeilijkheid bij de naleving van de transparantie-eis ligt in de wetgevende structuur en de bijzondere juridische cultuur. Ten eerste is de wetgevende macht verdeeld in meerdere niveaus; dit betreft zowel de wetgevende instanties als de bestuurlijke organen op lokaal niveau. Hoewel de hiërarchie van de wetgevende autoriteiten en hun bevoegdheden duidelijk lijken op centraal niveau, is de juridische status van wetgevende producten opgesteld door de lokale autoriteiten vaag omschreven. Dit is een belangrijke oorzaak van het probleem van niet-transparantie in Chinese wetgeving. Het ontbreken van een doeltreffend controle mechanisme houdt in dat tegenstrijdigheden tussen juridische documenten onopgelost blijven; dit leidt tot chronische wanorde in het formele juridische systeem in China. Ten tweede worden vaak normatieve documenten, die bestaan buiten het formele rechtssysteem als een reeks van informele wetten, door de bestuurlijke instanties op lokaal niveau opgesteld. De uitvaardiging is grotendeels willekeurig, zonder een juridisch correcte regulering van de rechtsgang. Bovendien zijn de documenten zelf meestal niet toegankelijk voor het publiek. Ten derde, het liberale beginsel van de *government accountability* ('de staatsmacht is gebaseerd op de wil van het volk'), waaruit het concept van transparantie wordt afgeleid, is niet meteen duidelijk in de Chinese juridische cultuur. In China is de wet een product van de wil van de overheid of de partij. Het bestuur wordt gevormd door een soevereine politieke autoriteit die grotendeels immuun is voor tegenspraak. Regels dienen als instrumenten van het controlebeleid van de partij en daarmee blijft alleenheerschappij van de partij gelden. Onder deze ideologie dragen bestuurlijke instanties verantwoordelijkheden voor de samenleving, maar zijn er geen verantwoording aan schuldig. Ze zijn alleen maar verantwoording schuldig aan hun politieke superieuren. Deze bijzondere juridische cultuur verzwakt de verantwoordingsplicht van de regering. Bijgevolg wordt het belang van transparantie ook verzwakt. Gehinderd door institutie-gerelateerde problemen, kunnen inspanningen van handelspartners die China aansporen om een landelijk tijdschrift in te stellen voor de publicatie van alle met de handel verband houdende wetten, voorschriften en regels, dus slechts beperkte resultaten bereiken op centraal niveau en nog minder op lokaal niveau.

Zoals aangetoond in hoofdstuk drie, vormt de spanning tussen lokale en centrale instituties ook een belemmering voor de uniforme toepassing van de uitvoering van de wet. Hoewel China grondwettelijk een unitaire staat blijft in institutioneel perspectief, is de macht in praktische zin verdeeld tussen het centrum en de periferie. Deze gefragmenteerde structuur is zichtbaar in de samenleving en zorgt voor algemene problemen in de nationale regelgeving. Bovendien kan het gefragmenteerde juridische systeem, in combinatie met de willekeurig en ondermaats gereguleerde juridische uitvoering door lokale overheden,

zorgen voor extra moeilijkheden bij de uniforme toepassing door de centrale autoriteit. Een illustratief voorbeeld van de gefragmenteerde aard van het staatsbestuur is het probleem van de versnippering van de markt. Eén geïntegreerde interne markt met vrij handelsverkeer is namelijk afwezig of zeer gebrekkig in China. De binnenlandse markt van China functioneert anders dan wat worden verwacht van een politieke unie met een centrale regering. Hoewel China een gemeenschappelijk buitenlands beleid kent, heeft het land geen geïntegreerde interne markt. Met het oog op een uniforme interne markt en eerlijke binnenlandse concurrentie, heeft de centrale overheid zich ingespannen om wetgeving op te stellen ten einde interne handelsbarrières weg te nemen. Echter, de wetgeving wordt niet daadwerkelijk toegepast op lokaal niveau en faalt in het beëindigen van de lokale handelsbelemmeringen. Terwijl de versnippering van de markt toegeschreven kan worden aan verschillende factoren in de economische en bestuurlijke systemen van het land, toont het voortbestaan ervan grotendeels de problemen van de centrale overheid om een uniforme administratie te realiseren bij de toepassing van de centrale wetgeving. Het ontbreken van een interne markt leidt tot aanmerkelijke verstoringen van de handel en belemmert China in het naleven van inhoudelijke WTO-verplichtingen. Het ontneemt het land de mogelijkheid om handelsmaatregelen te herzien in overeenstemming met de non-discriminatiebepalingen (nationale behandeling) zoals geformuleerd in the WTO. Aangezien Chinese producten al zijn onderworpen aan binnenlandse discriminerende behandeling, is de regel van nationale behandeling niet hanteerbaar. Het probleem van de versnippering van de markt manifesteert zich ook in een spanningsveld tussen nationale regelgeving en de wens om de lokale autonomie te stimuleren in het belang van de economische ontwikkeling. De WTO-lidmaatschap versterkt deze spanning door te eisen dat China meer economische activiteiten decentraliseert naar de lokale overheid - bijvoorbeeld buitenlandse investeringsmaatregelen - en op hetzelfde moment te verlangen dat een uniforme administratie wordt gevoerd en lokale activiteiten naar behoren worden afgestemd.

Hoofdstuk vier onderzoekt de functie van rechterlijke toetsing ter verbetering van een uniforme toepassing van de wetgeving. De toetsing wordt ondermijnd door structurele tekortkomingen in de Chinese gerechtelijke organen. De rechterlijke toetsing, een mechanisme ontwikkeld in westerse landen, betreft in wezen het systeem van controle en evenwicht uitgeoefend door de rechterlijke macht over de andere machten van een staat. Het is gebaseerd op fundamentele beginselen, zoals het concept van de rechtsstaat en de scheiding der machten. Dit concept vindt weinig weerklank in China. Er is geen scheiding der machten in China en, tot op zekere hoogte, zijn de justitiële organen ondergeschikt aan uitvoerende- en partijorganen. Het algemene probleem van een niet-onafhankelijke rechterlijke macht is vooral duidelijk bij rechterlijke toetsing die bestuursorganen uitdagen. Naast directe bemoeienis door bestuurs- en partijorganen, kiezen rechtbanken vaak voor terughoudendheid om confrontatie met bestuurlijke autoriteiten te voorkomen. Het uitzonderlijk hoge tempo van intrekking van zaken die zijn onderworpen aan rechterlijke toetsing, toont deze vrijwillige beperking. Rechters kunnen de eisers ervan overtuigen om

de rechtszaak op te geven door te suggereren dat er weinig kans is om te winnen en dat buitengerechtelijke bemiddeling een betere oplossing zou zijn.

Bovendien verergert de beperkte omvang van de rechterlijke toetsing het probleem veroorzaakt door de structurele gebreken en belemmert het rechtbanken bij het beoordelen van problematische bestuurlijke beslissingen. Rechtbanken zijn niet in staat om de wettigheid van de bestuurlijke regels te toetsen. China's uitsluiting van bestuurlijke regels van de werkingssfeer van de rechterlijke toetsing is een unieke praktijk, ook al is primaire wetgeving niet onderworpen aan rechterlijke toetsing door de gewone rechtbanken in de meeste rechtsstelsels. In veel gevallen is de toetsing van de wettigheid van regels essentieel om de wettigheid van bestuurlijke beslissingen, gebaseerd op die regels, te beoordelen. Op verzoek van de leden van de WTO heeft China getracht een speciale regel voor de rechterlijke toetsing van bestuurlijke beslissingen met betrekking tot de internationale handel te bieden. Door zaken voor te leggen aan hogere rechtbanken worden meer deskundige rechters ingezet die minder gevoelig zijn voor plaatselijke inmenging. Het feit dat er weinig gegevens kunnen worden gevonden over de toepassing van de regel, suggereert dat deze zelden wordt toegepast. Het kan gemakkelijk zijn voor China om een regel als tijdelijke verlichting voor handelspartners af te kondigen, maar dit zal moeilijk in praktijk te brengen zijn en het is onwaarschijnlijk dat er op de lange termijn significante resultaten zullen worden bereikt.

Door middel van de casus van ineffectieve handhaving van het intellectueel eigendomsrecht (IER) in China, laat hoofdstuk vijf zien hoe de problemen, die werden geconstateerd in de vorige drie hoofdstukken, doorwerken op een meer concreet niveau. Ten eerste is IER-gerelateerde wet- en regelgeving, evenals rechterlijke beslissingen, slechts selectief gepubliceerd en zijn er geen gevestigde en publiek toegankelijk tijdschriften of websites. Gebrek aan transparantie maakt het moeilijk om nauwkeurig de toepassing van IER-wetten te onderzoeken. Het ontbreken van transparantie draagt ook bij aan de onvoorspelbare en grillige bestuurlijke handhaving van het IER. Ten tweede ondermijnt het probleem van de versnippering de effectiviteit van de handhaving van het IER, vooral omdat handhaving afhankelijk is van een hoge mate van samenwerking tussen regio's en bestuursorganen. De samenwerking tussen organen wordt belemmerd door verticale fragmentatie, dat wil zeggen een groot aantal autoriteiten met vaag omschreven en overlappende rechtsbevoegdheden betreffende handhaving van het IER. De versnippering van bevoegdheden leidt in sommige gevallen tot het afschuiven van verantwoordelijkheden voor de handhaving en tot overlappende en ongecoördineerde handhaving in andere gevallen. De samenwerking tussen de regio's wordt belemmerd door horizontale fragmentatie, die vooral betrekking heeft op het probleem van lokale bescherming bij de handhaving van het IER. Economische afhankelijkheid van de industrie die inbreuk maakt op eigendomsrechten, motiveert lokale overheden om hun eigen economische belangen te laten prevaleren boven de bescherming van intellectuele eigendomsrechten. Bovendien ondermijnt de gefragmenteerde nationale overheidsstructuur en de autonomie van lokale overheden nationale inspanningen bij de handhaving van het IER. Ten derde toont het onderzoek van IER-gerelateerde rechterlijke

toetsingspraktijk aan dat, als gevolg van structurele tekortkomingen in gerechtelijke organen, individuen de rechterlijke toetsing weinig frequent inroepen als een remedie om onwelgevallige bestuurlijke beslissingen aan te vechten. De meerderheid van de IER-gerelateerde rechterlijke oordelen vindt plaats op centraal niveau, terwijl het aantal gevallen op lokaal niveau extreem laag is. Hoewel het moeilijk is om te bepalen in welke mate het gebrek aan onafhankelijkheid de effectiviteit van de rechterlijke toetsing ondermijnt, suggereert het extreem lage aantal gevallen op lokaal niveau dat IER-gerelateerde bestuurlijke beslissingen zelden worden aangevochten door middel van rechterlijke toetsing.

De complexiteit van de Chinese wetgeving, het versnipperde karakter van het bestuurlijke systeem en de structurele gebreken in de justitiële organen vormen aanzienlijke obstakels voor de naleving van de systeem-verplichtingen die voortvloeien uit de WTO. Inzicht in de institutionele belemmeringen waarmee China kampt, maakt het gemakkelijker om te begrijpen dat het opleggen van WTO-plus verplichtingen een irrationele strategie is en waarschijnlijk niet het gewenste resultaat zal hebben, aangezien het aan een zwakker lid hogere eisen stelt dan andere leden. Het zou naïef zijn om te denken dat het proces van aanpassing kan worden versneld door het uitoefenen van voldoende druk van buitenaf. Uitgebreide bestudering van het institutionele vermogen van een WTO-lid om te voldoen aan verplichtingen is de eerste stap op weg naar het vinden van een oplossing voor een betere integratie. China's zaak toont aan dat uitbreiding van het WTO-mandaat niet noodzakelijkerwijs het wereldhandelssysteem helpt om zijn effectiviteit te optimaliseren. Het eisen van naleving van diep ingrijpende regels door een lid als China vergt het uiterste van de bestuurscapaciteit van de WTO om een evenwicht te bewaren tussen liberalisering van de handel en autonomie van de nationale regelgeving. Hoe tegemoet te komen aan de sterke juridische en politieke beperkingen van ontwikkelingslanden zal een van de meest uitdagende taken zijn voor de hervorming van het wereldhandelssysteem.

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